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Politics this week

Oct 26th 2006
From The Economist print edition

AP

Iraq remained the dominant issue in America's **mid-term elections**. With less than two weeks to go before polling day, Democrats hammered home the message that October is already the deadliest month of the year in the conflict both for American troops and Iraqi civilians. George Bush acknowledged his own dissatisfaction but said America was constantly adjusting its strategy and still winning. See article

In **Iraq** itself, the prime minister, Nuri al-Maliki, pledged to crack down on illegal militias, particularly the Shia Mahdi Army, that are responsible for most of the continuing sectarian violence. But he refused to set a timetable for this; Shia parties with links to the militias make up part of his own coalition government.

New Jersey's highest court issued a mixed ruling on gay marriage. It decided that homosexual couples are entitled to the same rights as heterosexual ones, but it avoided a conservative backlash (for now) by giving the state legislature time to ponder whether this constitutes “marriage”.

The **Mark Foley** scandal rumbled on as Dennis Hastert, the Speaker of the House of Representatives, presented his version of events to the House ethics committee. The committee's report on Mr Foley's relationship with congressional pages is expected soon.

California's department of corrections provided the first details of its plans to house some prisoners temporarily in other states. Arnold Schwarzenegger, the state's governor, issued an emergency proclamation earlier this month in response to “severe overcrowding” in prisons.

Making nice

Iran's fiery president, Mahmoud Ahmadinejad, who has called for Israel to be “wiped off the map”, threatened that European countries could get “hurt” unless they distanced themselves from the Jewish state. Meanwhile, unfazed by discussion of UN sanctions over its refusal to suspend suspect uranium-enrichment work, Iran said it would inject uranium gas into a second cascade of enrichment machines at its plant at Natanz.

Israel's coalition government tilted towards the right after the prime minister, Ehud Olmert, was forced to accept the inclusion in its ranks of the right-wing Yisrael Beitenu Party, led by Avigdor Lieberman. The decision is meant to ensure the government's survival following the war in Lebanon over the summer, widely seen as a disaster. See article

The head of the United Nations mission to **Sudan**, Jan Pronk, was expelled from the country by the government. His offence was to write in his blog that the Sudanese army has suffered some defeats in Darfur against rebel fighters and that its morale is low.

The capital of **Chad**, N'Djamena, was fortified following reports that rebels were moving towards it from the east of the country. The government of President Idriss Déby, which survived a rebel assault on the city in April, accuses neighbouring Sudan of arming and backing the rebels.

The prime minister of **Ethiopia**, Meles Zenawi, said that his country was now “technically at war” with the Islamist militias that have taken over much of neighbouring Somalia. Ethiopia has admitted to having hundreds of troops in the country in support of the weak transitional government based in Baidoa. See article

Devil in the detail

North Korea's regional neighbours continued their consultations about how to impose sanctions on the country following its nuclear test earlier this month. Pyongyang rattled its sabres and warned South Korea that if it participated in the UN-backed sanctions this would be a “declaration of confrontation”. See article

India's prime minister, Manmohan Singh, appointed Pranab Mukherjee as foreign minister. Mr Singh had been doing both jobs since last November, when his then foreign minister resigned over the Iraq oil-for-food scandal.

Russia's way

Russia's president **Vladimir Putin** had a stormy few days after an open microphone caught him praising Israel's president for his virility in multiple alleged rapes. He also had a prickly meeting with European Union leaders in Finland, where they pressed him to liberalise his country's energy market, and came under pressure over **Georgia**. In a national phone-in, Mr Putin underlined his anger with Georgia, accusing the authorities there of resolving problems “by force”. See article

Germany's armed forces are likely to have a more robust role overseas. The government approved a new security doctrine that reaffirmed the Atlantic alliance, but foresaw wider involvement in peacekeeping. Existing rules restrict German troops in Afghanistan from fighting the Taliban. See article

In **Hungary**, violent clashes between police and demonstrators demanding the government's resignation marred the commemoration of the 50th anniversary of the anti-Soviet 1956 uprising. Police used tear-gas against the protesters and more than 100 were hurt.

AP

Britain announced restrictions on migrants from **Romania** and **Bulgaria**, which join the EU next year. The restrictions were criticised by both free-marketeers and protectionists, but only six EU countries have said, so far, that they will fully open their labour markets to the workers. See article

Wider still and deeper

In a referendum 78% of those voting approved a $5.2 billion plan to widen and deepen the **Panama Canal**. The expansion, due to be completed by 2014, could turn Panama into the logistics hub of the Americas, according to its backers.

Mexico's Senate rejected a call to sack the governor of the southern state of Oaxaca, which has had its capital disrupted by striking teachers and left-wing protesters for the past five months. The governor's supporters have called for federal police to evict the protesters.

AFP

After dozens of rounds of voting at the **United Nations General Assembly** for one of the two Latin American rotating seats on the Security Council, Guatemala out-polled Venezuela, but failed to secure the required two-thirds majority. The search began for a compromise candidate.

Bolivia's government agreed to give jobs in a revived state-owned mining firm to 4,000 self-employed miners involved in clashes over a tin deposit earlier this month in which 16 people were killed and 60 injured.

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Business this week

Oct 26th 2006
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Jeffrey Skilling, Enron's former chief executive, was sentenced to more than 24 years in prison and ordered to pay $45m in restitution for his part in the fraud that bankrupted the energy trader in 2001. Mr Skilling was found guilty in May along with Kenneth Lay, but Mr Lay's convictions were recently “vacated” following his death in July. Enron employees who lost their pensions expressed satisfaction at Mr Skilling's sentence. He said he was innocent and would appeal against the verdict. See article

The former chief financial officer of **Comverse Technology** pleaded guilty to fraud in relation to a **stock-options scandal**. He was the first senior executive to plead guilty in a host of similar scandals that have recently come to light, though other big corporate cheeses have resigned from their jobs. Comverse's former boss, Jacob “Kobi” Alexander, who fled America, is fighting his extradition from Namibia.

The retrial began of **Josef Ackermann**, the chief executive of Deutsche Bank, and five others who face criminal charges that stem from the awarding of executive bonuses at Mannesmann. Mr Ackermann was on the company's supervisory board at the time of its takeover by Vodafone in 2000 (Deutsche Bank is not connected to the trial). There is speculation that Mr Ackermann will plead guilty to non-criminal charges in order to concentrate on running Germany's biggest bank.

Pick up a Penguin

United Biscuits, which makes some of Britain's best-known snacks, including Jaffa Cakes, Penguin biscuits and Hula Hoops, agreed to be bought by two private-equity firms for some £1.6 billion ($3 billion).

Altria announced that it would reveal its decision on whether (and how) to spin off **Kraft Foods** at a shareholders' meeting in January. The conglomerate has long wanted to sell Kraft, but its plans were put on hold after its Philip Morris unit became embroiled in tobacco litigation.

Carl Icahn won his battle to shake up the management of **ImClone Systems**, a biomedical company, when it appointed him chairman and sacked its interim chief executive. Mr Icahn, who owns around 14% of the company, had led a shareholders' campaign to oust several directors.

First, the bad news

Ford reported its biggest quarterly loss in 14 years—$5.8 billion—as it booked writedowns and charges. The performance of Ford's North American auto unit, where sales dropped by some 15% compared with a year ago, and its premier-car group, which includes Jaguar, continued to pull down its earnings. Alan Mulally, who was appointed Ford's chief executive in September, said the results were “unacceptable”.

DaimlerChrysler's quarterly profit, 37% lower than a year ago, was also hampered by plunging sales in America, offsetting an improved performance at the company's Mercedes unit. But there was some good news for Detroit when **General Motors** said a net loss of $115m (compared with $1.66 billion last year) was actually an adjusted profit of $529m if special items, which are related to its restructuring, were excluded.

Some much-needed good news for **Airbus**. It sealed a deal to set up a plant in China and won an order for 150 A320 jets from the country.

A substantial merger was announced in Australia's insurance industry as **Promina** agreed to a A$7.9

billion ($6 billion) takeover proposal from **Suncorp-Metway**, a rival which also operates banks.

In an unusual move for the company, IBM filed two lawsuits against **Amazon** claiming the online retailer infringed five patents on internet technology, including processing online transactions. IBM holds more patents than any other American company and usually seeks to resolve licensing disputes out of court.

Meanwhile, **Amazon** said its quarterly profit had fallen (again). But as sales exceeded forecasts, its share price rose. Investors also cheered Amazon's statement that it would put a brake on buying new technology that has enabled it to launch services such as film downloads, but dragged down earnings.

Sony's net profit plunged by 94% in its second quarter (and it made an operating loss) compared with a year ago. Along with the continuing troubles at its gaming unit, the conglomerate took a hit from the safety recall of 9.6m laptop batteries, for which its executives apologised. See article

Only bricks and mortar

Existing-home sales in America slid in September for a sixth month as the housing market continued to slow. The median home price also fell, to $220,000—2.2% less than a year ago. But the fall was bigger in some regions—5.1% in the north-east for instance.

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Iraq

Cut and run?

Oct 26th 2006
From The Economist print edition

America's voters are entitled to punish George Bush. They should not punish the people of Iraq

Get article background

WHEN a great democracy such as the United States holds elections at a time of war, voters are torn between two instincts. One is to show grit and solidarity by rallying around the flag and the president. The other is to treat the election as a referendum on the war. Ever since September 11th 2001 George Bush has milked the first instinct for all it is worth. But having gained so much from presenting himself as a war president, Mr Bush can hardly complain now that the voters are moving in the other direction. Many seem intent on using November's mid-terms to give their verdict on his handling of the war in Iraq. That is bad news for the Republicans. According to a Gallup poll this week, only 19% of Americans still think that America is winning. In Britain, America's chief ally in Iraq, the disenchantment is deeper. An ICM poll this week found that 45% of Britons wanted their troops to leave at once, and a further 16% wanted them out by the end of the year.

Patience and its limits

This loss of faith among the people of Britain and America is easy to understand. They have already shown a lot of patience. More than three years after the overthrow of Saddam Hussein, Iraq has become progressively more violent (see article). Some 2,200 American soldiers and 120 British ones have been killed, and the death toll among Iraqis may stretch into the hundreds of thousands.

Voters in the West would be steadier if they believed Iraq to be heading, however fitfully, in broadly the right direction. But that is not certain. Free elections have been held, but these have not yet brought effective government. A constitution has been written, but this has not resolved the big differences between Shias, Sunnis and Kurds. Especially since the bombing of the Shias' Askariyah mosque in February, the violence has mutated from a low-level insurgency into a sectarian civil war, with ethnic cleansing already under way in some areas. George Casey, America's top general in Iraq, did his best this week to express some cautious optimism. Zalmay Khalilzad, the American ambassador in Baghdad, insisted that success was still possible. But plenty of other diplomats and generals (including the head of Britain's army) have taken a more sombre view. Iraq may have bottomed out, or the worst may be yet to come. The truth is that nobody knows for sure.

In recent weeks the combination of an election campaign in America with the lack of progress in Iraq has for the first time produced a vigorous, open debate about strategic alternatives. Yet the benefits of this debate may turn out to be more apparent than real. For none of the alternative ideas mooted so far, such as partition, installing a strongman or withdrawing American forces “over the horizon”, looks more promising than the existing three-part strategy. This, broadly, is to damp down the violence as much as possible while continuing to train Iraq's own soldiers and policemen and pressing Iraq's elected politicians to make a power- (and oil-) sharing deal that could end the civil war. The real choice facing America and its allies in Iraq is whether to persevere with this strategy in the hope of eventual success, or admit failure now and start to head for the exit.

For the politicians (and newspapers, like ours) who argued strongly for the invasion of Iraq, it is no longer enough to accuse those who want to head for the exit of “cutting and running”, as if using a pejorative phrase settled the argument either way. Cutting your losses is sometimes the sensible thing to do, even for a superpower, and even after paying a heavy price in lost lives and wasted money. If you genuinely believe, as many people now do, that the likeliest long-term outcome in Iraq is that America will end up cutting and running anyway, with no improvement to be expected even three or four years hence, why simply postpone the inevitable?

Because failure may not be inevitable. It is true that Iraq is not poised to become the exemplary democracy the American neocons dreamed of carving out in the heart of the Arab world. But that definition of success was always a peculiar one to apply to a war the United States launched primarily to secure its own interests. A failure to turn Iraq into Switzerland means neither that Iraq is fated to collapse altogether nor that its people are doomed to perpetual fratricidal war. The question Americans need to ask is what impact their own staying or going is likely to have on the balance of probable outcomes. And in answering this question, the case for staying becomes a good deal stronger. By persevering, America stands at least some chance of putting Iraq on a more stable trajectory. By leaving, it is almost certain to make things worse.

What you can't do once you've gone

At a minimum, America's continuing presence in Iraq prevents the neighbours from joining in a civil war, as Lebanon's neighbours did in the 1970s with much less at stake. The Americans can still move into and establish some order in areas where the violence surges out of control. They can protect the elected government and put pressure on its members to make a political settlement. They can continue to train Iraq's own security forces and, if necessary, attack or dismantle some of the militias. Once they leave they can do none of these things. Senator John Warner spoke for many when he worried recently that the situation was “drifting sideways”. But there are worse directions than sideways. Leaving now stands a fair chance of plunging Iraq into an enlarged war and a far bigger bloodbath than anything seen so far.

For Mr Bush, the Iraq war has in one sense already been lost, whatever result the mid-terms bring. This president's legacy will forever be tainted by what he overpromised and how much he underperformed. The voters of America are entitled to judge and punish his party as they see fit. But Americans would be wrong to extend this punishment to the people of Iraq, who have suffered so much already. Even if it was a mistake to blunder into Iraq, it would be a bigger mistake, bordering on a crime, for a nation that aspires to greatness to blunder out now, without first having exhausted every possible effort to put Iraq back together and avert a wider war.

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European politics

What France needs

Oct 26th 2006
From The Economist print edition

France is in a similar funk to Britain in the 1970s: a Madame Thatcher could restore its confidence

THERE is a palpably sour mood in France these days. As Jacques Chirac enters the twilight months of his 11th and (surely) final year as president, he is the most unpopular occupant of the Elysée Palace in the fifth republic's history. The government of his prime minister, Dominique de Villepin, has been paralysed ever since street protests forced it to withdraw a modest labour-market reform in the spring. The French have invented a buzzword: declinism, summing up the belief that the country is unreformable.

France matters. It is the world's sixth-biggest economy, a permanent member of the UN Security Council and a declared nuclear power. It was a founder of today's European Union, a driving force behind the creation of the single currency and—despite French voters' rejection of the draft EU constitution in May 2005—a longstanding promoter of deeper European integration. It is in part thanks to France's paralysis that the union is itself so uncertain of its direction. That is why Europe and the world are watching with close interest as the campaign for next spring's presidential election unfolds.

Our survey this week explains the gloomy background to that election. For ten years in a row, the economy has grown by less than the rich-country OECD average. The public finances are looking wobbly: public spending accounts for half of GDP, and in the past ten years the public debt has increased faster as a share of GDP in France than in any other EU-15 country. Above all, France suffers from stubbornly entrenched unemployment, which seems stuck at 8-10% overall, and over 20% for the young. It was chronic joblessness, as much as anything else, that lay behind the riots and car-burnings that exploded in the *banlieues* of Paris, heavily populated by disaffected Muslim youths, exactly a year ago. Today, these neighbourhoods remain tense: 21,000 vehicles were burned in the first six months of this year alone—twice as many as during the three weeks of rioting. A sense of exclusion lingers.

It's not impossible

Yet France is a country of contradictions. Its economy may be sluggish, but its workers are among the world's most productive. Its people are famously leery of globalisation and economic liberalism, yet France boasts some of the world's most successful multinational companies. Its public sector may be bloated and its tax burden excessive, yet the quality of its public officials is widely admired. Its mass-education universities come deservedly low in the world rankings, yet Paris's famous *grandes écoles* are among the best in the world. In short, France is a place in which, for almost every weakness, it is

possible to find a matching strength.

The question is whether France can now build on these strengths by bringing in pro-competitive reforms—to its labour market, to its protected utilities and public monopolies, to its social model, to its public services and to its stifling regulatory system. There are reasons to be optimistic. Many of France's impressive businessmen are demanding change. The country's demographic outlook is healthier than its neighbours. Because it is less dependent on manufacturing than Germany, Italy and Spain, France has less to fear from low-cost Asian competition. It will always be hard to get reforms past the gauntlet of France's street protesters. But at least the government is not hobbled by the scratchy coalition politics that bedevils all attempts at reform in Germany and Italy.

And others have led the way. World-weary French commentators sometimes maintain that only smaller, more homogenous countries, such as Ireland, Finland, Denmark or the Netherlands can reform. But Spain has opened up its economy and Canada has restored its public finances. And look across the channel: in the 1970s Britain was suffering from declinism too. Many said that the trade unions were too strong, that reform was impossible. After all, one prime minister, Edward Heath, had made a valiant attempt at change in 1970-72, only to be unseated by a miners' strike—rather as Alain Juppé's bold reforms in 1995-97 were overturned by street protests. And yet after 1979 Margaret Thatcher showed that a determined government could shake up a sclerotic economy (and defeat the miners). It was a matter of leadership, above all.

The choices in spring

The real issue is not whether France is reformable—for the answer must be yes. It is whether there is a Madame Thatcher who has the courage to take on vested interests. The prognosis is not encouraging. On the left, three candidates will contest the Socialist Party's presidential nomination on November 16th. Even the most moderate, Dominique Strauss-Kahn, has signed up to an old-style socialist programme. Another, Laurent Fabius, has refashioned himself as a champion of the people against “hypercapitalism”. The front-runner and supposed moderniser, Ségolène Royal, has criticised the absurd rules on a 35-hour working week—but only for giving employers too much power over workers. On the right, Nicolas Sarkozy, the hyperactive interior minister, looks more promising. He preaches a “rupture” with past policies and an overhaul of the “social model”. Yet he was an interventionist finance minister with no apparent love for free markets, and has recently sounded softer on the need for radical reform.

Unpromising material, but then France's *dame* or *homme de fer* does not need to be quite as ironclad as the former British prime minister. When Mrs (now Lady) Thatcher embarked on her mission to convert Britons to the joys of wealth creation, Leonid Brezhnev led the Soviet Union and many still dreamed of a socialist Utopia. By contrast, France's hostility towards capitalism may be skin-deep—kept alive chiefly because politicians like Mr Chirac pander to it instead of confronting the French public sector with the realities of a global economy in which its private sector flourishes.

In Britain, where the private sector was much weaker, it took nearly two decades to turn around the economy. If the next French president can push through the reforms needed to restore the country's competitiveness, France could rebound far more quickly than the *déclinologues* assert.

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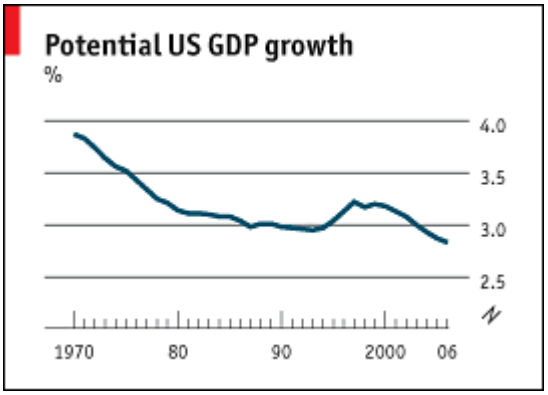
America's economy

A falling speed limit

Oct 26th 2006
From The Economist print edition

America's long-term rate of growth may be slowing; that will make its economy harder to run

Get article background



THE world is used to the idea that America's economy grows much faster than Europe's, because that is the way it has been for many years. But it may not be that way for much longer. Just as European growth seems to be picking up, perhaps to over 2% a year, America's appears to be heading downwards to not much more than that.

In the short term America's economy is certainly slowing, as the latest GDP figures, due out on October 27th, are expected to show. But the more worrying data concern the longer term. America's economic speed limit—the pace at which the economy can grow without fuelling inflation—is also dropping. It may soon be as low as 2.5% a year, by some estimates the slowest pace in more than a century.

Watch that accelerator

An economy's potential or trend rate of growth depends on the supply of workers and their productivity. The productivity boom that began in the mid-1990s pushed America's trend growth rate well above 3% a year. Now it is falling, both because the productivity surge is fading and because the supply of workers has slowed (see article). The baby-boomers are approaching retirement. Women's rush into the workplace has at least slowed, and may have reversed. Teenagers are working less. And hostility to immigration, another source of labour, is rising: witness the barriers along the Rio Grande.

Any fall in America's economic speed limit will have serious consequences. Financial markets could be rattled as investors lower their expectations for future profit growth. American assets may look less attractive to foreigners. And economic policy will become decidedly more complicated.

It will be particularly awkward for central bankers. America's underlying inflation rate is already uncomfortably high. For inflation to fall, the economy needs to grow below its trend rate, but if that rate is dropping, the Federal Reserve's task becomes harder: raise interest rates too far and recession looms; do too little and inflation worsens. The failure of central bankers to recognise that the economic speed limit had dropped was one reason why inflation spun out of control in the 1970s. Fortunately, their successors seem determined not to repeat that mistake. Some evidence suggests the Fed's officials are lowering their estimates of potential growth faster than many on Wall Street. At their policy-setting meeting this week, the central bankers kept short-term interest rates unchanged at 5.25%, but repeated their warnings about “inflation risks”.

Politicians' lives will get harder too. Slower growth means less tax revenue and a darker fiscal outlook. Official estimates of America's long-term budget problems, such as the shortfall in the Social Security pension system, may not change, since they are already based on very gloomy assumptions about productivity growth. But if productivity growth slows and a smaller share of people work, the burden of paying for the health care and pensions of the baby-boomers will increase.

Reforming health care and pensions will therefore become more urgent—but also harder. Slower growth tends to sour the political environment. Populist solutions gain appeal. There is a danger that, instead of

pushing policies that boost America's potential (such as encouraging old folk to work longer, boosting the number of immigrants and freeing trade), politicians will turn to easy protectionist solutions. Which would, of course, slow the economy further.

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Wrong model, right continent

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China knows what it wants from Africa and will probably get it. The converse isn't true

AFP

THE characters for “Africa” in the Mandarin language mean “wrong continent”. But the Chinese have often ignored this etymological hint. In the 15th century the emperor's emissaries sailed as far as Mozambique, carrying silk and returning with a giraffe. In the cold war Maoists dotted Africa with hospitals, football stadiums and disastrous ideas.

Next week China will host more than 30 African leaders from the wrong continent in Beijing, offering them a pinch of debt relief, a splash of aid, plus further generous helpings of trade and investment. China already buys a tenth of sub-Saharan Africa's exports and owns almost $1.2 billion of direct investments in the region (see article). A Chinese diaspora in Africa now numbers perhaps 80,000, including labourers and businessmen, who bring entrepreneurial wit and wisdom to places usually visited only by Land Cruisers from international aid agencies.

What is in it for China? It no longer wants Africa's hearts, minds or giraffes. Mostly, it just wants its oil, ores and timber—plus its backing at the United Nations. Thus, even as the Chinese win mining rights, repair railways and lay pipelines on the continent, Africa's governments are shuttering their embassies in Taiwan in deference to Beijing's one-China policy.

This suits Africa's governments. The scramble for resources invariably passes the ministerial doorstep, where concessions are sold and royalties collected. China helps African governments ignore Western nagging about human rights: its support has allowed Sudan to avoid UN sanctions over Darfur. And some Africans look on China as a development model, replacing the tough Washington Consensus with a “Beijing Consensus”: China's economic progress is cited by statists, protectionists and thugs alike to “prove” that keeping the state's grip on companies, trade and political freedoms need not stop a country growing by 8%-plus a year.

Think again, Africa

The Chinese part of this puzzle is easier to deal with: even if it is not the first resource-hungry power to behave poorly in Africa, China should be condemned wherever it bribes, cajoles or (in the case of Sudan) permits genocide. But what about the African hope that China provides an economic model?

Sadly, China's success is an obstacle, as well as an inspiration. Its rise has bid up the price of Africa's traditional raw commodities, and depressed the price of manufactured goods. Thus Africa's factories and assembly lines, such as they are, are losing out to its mines, quarries and oilfields in the competition for investment. Even if Africa's labour is cheap enough to compete with China's, its roads, ports and customs are far from good enough. If they are to provide jobs for their workers, not just rents for their governments, Africa's economies must find less-exposed niches in the world economy, such as tourism or cut flowers. And they should look not to China, but to Chile or Botswana for examples of how to turn natural bounty into shared prosperity.

China is doing its bit to improve infrastructure, building roads and railways. But it could do more to open up its own markets. China is quite open to yarn, but not jerseys; diamonds, but not jewellery. If it has as much “solidarity” with Africa as it claims, it could offer to lower tariffs on processed goods. Chinese firms have also ignored international initiatives to make project finance greener (the “Equator Principles”) and to make mining industries cleaner (the “Extractive Industries Transparency Initiative”). Even with China's backing, these outside efforts might not succeed: honesty and greenery come from within. Without it, they will certainly fail.

For their part, Africa's leaders could also play their hands rather better. They should talk to each other as well as their hosts in Beijing. If they negotiated as a block, they could drive a harder bargain. Just as China insists that foreigners enter into joint ventures with its companies, so Africans should make sure they get China's know-how, not just its money.

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Brazil's presidential election

Wanted: a champion for privatisation

Oct 26th 2006
From The Economist print edition

Lula's campaign augurs ill for economic reform

AP

THE smart money had long since bet that Luiz Inácio Lula da Silva would win a second term as Brazil's president in a general election held on October 1st. But at the last moment his candidacy was tripped up by the dumb money—piles and piles of it, apparently to be used by his Workers' Party to smear an opponent in a gubernatorial race. It reminded Brazilians that Lula, as they call him, presided over a much bigger corruption scam involving cash for votes in Congress. It was enough to force a run-off vote, to be held this Sunday, against Geraldo Alckmin, a former governor of São Paulo.

Having come within seven percentage points of Lula, Mr Alckmin has since lost ground. The opinion polls suggest once again that Lula is cruising to victory (see article). His opponent is a dull technocrat. Most Brazilians believe the president is not personally corrupt. They give him credit for a huge anti-poverty programme and for preserving economic stability.

But Lula has restored his lead partly by campaigning against the privatisations carried out by Mr Alckmin's party when in power under Fernando Henrique Cardoso from 1995-2002. He accused his opponent of wanting to privatise such national heirlooms as Petrobras, the oil company, three big state banks and an electricity giant. The hapless Mr Alckmin felt obliged to insist that such a thought had never crossed his mind. To prove it, he donned a ridiculous jacket emblazoned with the logos of Brazil's corporate state. So the case for privatisation has gone by default—which is a pity.

Privatisation is certainly unpopular in Latin America. Voters think the sell-offs have benefited the new (often foreign) owners, not consumers. In some public utilities in some countries that is true, because governments failed to ensure adequate competition and regulation. But an authoritative study published last year by the Centre for Global Development, an independent think-tank in Washington, DC, found that privatisation in Latin America had been unfairly criticised and that although some firms had raised prices “the bottom line is still one of absolute gains for the poor.”

The Brazilian case for reform

Those gains are especially clear in Brazil. Before privatisation, obtaining a telephone meant waiting for years or paying $4,000 in a grey market. Phones were only for the rich. In just eight years since privatisation the number in service has more than quintupled. In private hands, the steel industry, Embraer (a planemaker) and CVRD (a mining giant) have become world-class competitors.

The next government would do well to restart privatisation. The state still owns around a third of the banking system. There is a case for a state-owned bank, since private ones have been poor at lending to farmers or setting up in remote areas. But three of them, all giants? Privatising the federal savings bank or the Banco do Brasil would allow the government to pay off a big chunk of public debt. That would allow interest rates to fall, halt the over-appreciation of the real and help to spring the economy from its low-growth trap.

The candidates' rejection of privatisation would be understandable if the economy were powering ahead. But the country lags on many indicators of competitiveness, thanks to a profligate public sector and pension system. If Lula wins, he should lead a debate about the economic reform Brazil sorely needs. This campaign has not provided it.

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About sponsorship

On talent, veils, America's population, gun control, Russia, Kazakhstan, the National Health Service, lying politicians

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From The Economist print edition

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Lack of ability

SIR – I disagreed with the basic premise of your survey on talent (October 7th). Contrary to what you say, there is absolutely no shortage of talented people, which is neatly demonstrated by the explosion of new technologies and businesses in the past 15 years. What we do have, however, is a problem of mismanaging talent. Companies simply do not know how to use the talent they have. Worse, they do not even know what they have. We could cite many explanations for this, but the biggest is the lack of a credible system to account for talent. It has taken more than 500 years to develop a solid accounting system for the old economy, but we cannot afford to wait even another 50 to develop a system for the new knowledge-based economy. It is important that all interested parties, including government, collaborate in developing a valid and transparent system for this new economy.

Meir Russ
Associate professor of business administration
University of Wisconsin
Green Bay, Wisconsin

SIR – The biggest problem in trying to retain talent is that employees tend to be rewarded not for innovation but for how well they play the company game. Companies that are forever reorganising, employ managers who prefer teams based on a “personality cult” and have review systems that are easily manipulated by the reporting manager, tend to reward those who can figure out internal politics more than problem solving, innovation or team building. Indeed, the innovative talent a company thinks it has built up is different to the talent of people to merely advance and survive.

William McNamara
Snohomish, Washington

SIR – Talent should not be viewed as a “commodity”. It is more like a product that has value added. Just as a car is not a commodity but a product made up of constituent parts, so talent is the end product of many complex elements. Talent increases in an individual through experience and the application of education, whereas commodities diminish in value over time: coffee, once drunk, is spent. Commodities are valuable because of the uses to which they are put (steel into cars). Talent, on the other hand, continues to grow throughout the life of its owner in proportion to the uses to which it is put.

Lorenz Jorgensen
Saffron Walden, Essex

SIR – I think you confused fact and fiction. You stated that the battle for talent lies in attracting people “like Aldous Huxley's alphas in ‘Brave New World'—those at the top of the bell curve”. This is wrong. The top of the bell curve is the average level. The best brains will be found at the right end of the curve.

Juemin Xu
Guildford, Surrey

SIR – You reported that three-quarters of senior human- resources managers consider “attracting and retaining” talent to be their “number one priority”. What on earth is the number one priority of the other

25%? Sack 'em, I say.

Timo Hannay
London

A veiled threat?

SIR – The current debate in Britain about the rights and wrongs of whether a Muslim woman should cover her face with a veil overlooks the fact that in many Muslim countries, non-Muslims (including temporary residents) are legally or socially required to adhere to local cultural norms ("Deconstructing the veil", October 14th). Such norms include forbidding the consumption of pork and alcohol; requiring women to be covered down to their wrists and ankles; banning men from wearing short trousers; and prohibiting the observance of non-Islamic faiths and the wearing of non-Islamic religious symbols. In multicultural and tolerant Britain is it really too much to ask that the norm of face-to-face communications be respected?

Bruce Guy
London

SIR – When historians look back on this period they will express incredulity that so much heat could have been generated over an item of clothing that so few Muslim women actually wear. I am not surprised that Muslims feel under threat. They are constantly given a negative coverage by the media but rarely accorded the proper chance to respond. No other group of adults in Britain has its dress code questioned this way. Why aren't mainstream politicians providing more reassurances to Muslims that they are welcome?

Adrian Waters
High Wycombe, Buckinghamshire

Middle-aged spread

SIR – I was disappointed that you, like other media, focused on births when discussing the burgeoning population in the United States ("Now we are 300,000,000", October 14th). Although you noted that births are neither increasing nor shrinking, and pointed out the fallacy of assuming that America's population growth is thus due strictly to immigration, you didn't let the other shoe drop. If births don't add to the population, and immigration isn't the whole story, accounting for around half of net population growth, where does the rest of America's growth come from?

The answer lies in improvements to mortality; people are not dying as soon as they used to. Consider that the bulk of the net growth in population is among older people. In the first half of the 21st century the number of Americans aged over 45 is projected to grow nearly three times as fast as the number under 45. Therefore the media has misrepresented what America's "young" economy will look like. People over 45 have more discretionary income than younger people. It is the older generation's spending, on more health care and travel but fewer flashy gadgets, that will create jobs and be the impetus of the new economy.

Martha Farnsworth Riche
Fellow, Centre for the Study of Economy and Society
Cornell University
Ithaca, New York

SIR – The optimism regarding America's population growth is unfounded. The world's present population of 6.5 billion already exceeds the world's biological carrying capacity and is projected to reach 9.3 billion by 2050. Moreover, each American currently has around six times the ecological footprint of his African or Asian counterpart and twice the footprint of Europeans. On current trends population growth is clearly unsustainable. In fact, the declining populations in Europe, Japan and other developed countries are one of the few positive signs in an otherwise bleak planetary future.

Phil Chubb
North Vancouver, Canada

Bullet point

SIR – So some in America think that three school shootings in a few days makes the case for more gun-control policies ("The horror", October 7th). They conveniently forgot that these three shootings were in fact four, the first being in heavily gun-regulated Canada the week before.

Matt Cooper
Oakland, California

A flailing state

SIR – Your clear-headed analysis of the contemporary state of Russia and the comparison to German politics in the inter-war period is appropriate ("The hardest word", October 14th). But there is another parallel between the two situations that you didn't mention. In 1919 lands that were formerly a part of Germany were stripped away, leaving it surrounded by small, weak states with sizeable, unhappy German minorities. This created an opportunity for the Nazis to exploit their aggressive territorial revisionism. Let us hope that the remarkable similarities between Germany then and Russia now will not lead to similar outcomes.

Nathaniel Kent
London

SIR – The rubric to your article said the piece was partly about a political "grudge" with Chechnya. But a bigger grudge was displayed in your cold-war-era journalism that used human tragedy to advance a political agenda. You say it may "be time to use the f-word"—fascism—in conjunction with Russia. I doubt the f-word I would use in response to that would get past your editors. A simple plea might do: leave Russia alone.

Ivan Ostervenely
Moscow

The wrong response to Borat

SIR – Thank you for highlighting Kazakhstan's crumbling health-care system ("An apple a day…", October 14th). As a native of Shymkent I've observed the unfolding scandal over the infection with HIV of children in the city's hospitals. The helpless parents have received little assistance and I am quite dismayed by the government's priorities. It seems to spend more time employing PR firms to protect its image against a hoax Kazakh journalist created by a popular British comedian than getting the country's health system in order.

Nurzhan Zhambekov
Washington, DC

Study report

SIR – We at *Health Service Journal* are quite aware of the limitations of our research on independent treatment centres (ITCs) ("Demonstration effect", September 30th). Much of the information needed to assess ITCs' value for money has been withheld on the ground of commercial confidentiality. We have looked instead at how much work has been carried out, compared with the amount needed to deliver the contract evenly. Our analysis pointed out that these contracts may allow for less work to be done in the initial period—information that was also denied us. What we do know about the cost of work done suggests that if there is any switching to higher value procedures, it has had a marginal effect. We conclude that the programme has got off to a slow start and that some centres are struggling. With limited information being put in the public domain about the ITC programme, we hope our research has opened up debate about its costs and benefits.

Nick Edwards
Editor
Health Service Journal
Market Harborough, Leicestershire

We get what we deserve

SIR – For a moment your leader on the governments of ex-communist Europe had me confused

(“Europe's fraying fringe”, October 14th). “Weak, deceitful, clownish, boorish, squabbling, thuggish and corrupt” could just as easily be used to characterise Berlusconi, Chirac, Kohl, Le Pen, Schröder and scores of their pals. The fact is that “sleaze and racism...eccentricity and petulant incompetence...and blatant lying” are pretty much the order of the day in all of Europe and the United States. West Europeans should indeed be shocked, not because they are so different from east Europeans, but because they are exactly alike.

Alexander Motyl
Professor of political science
Rutgers University
Newark, New Jersey

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Strategy in Iraq

Coming to the end of options

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From The Economist print edition

As the situation in Iraq deteriorates, George Bush may be pondering a new strategy. But, if so, it will not be revealed until after the mid-term elections

AP

Get article background

A MAN walks up to a shrub and asks: “So, what's our exit strategy from Iraq?” The voice-over intones: “OK, it's kind of ridiculous to think you're ever going to get an answer from this bush.” A picture of the president appears on the screen. The voice-over continues: “But it's also kind of ridiculous to think you're going to get an answer from this one.”

Amid the hubbub of an American election campaign, the loudest voices discussing Iraq are rarely the most constructive. Democratic ads linger over the graves of American soldiers. Republican spots feature the sound of a ticking bomb and a quote from Osama bin Laden about every Muslim's sacred duty to kill Americans.

Such commercials may be short on answers but, for all their crudity, they raise the questions that most trouble American voters: “Are we winning in Iraq?” and “If not, what on earth can we do about it?” In a *Newsweek* poll published this week, 31% of respondents—a plurality—said the situation in Iraq was the most important issue affecting how they will vote on November 7th. Even in military towns, the mood is troubled and frustrated (see article).

There is little doubt how Iraq will affect the American election. The same survey found that 46% of Americans think the Democrats would do a better job of handling Iraq than the Republicans, with only 34% believing the opposite. Stuart Rothenberg, a political analyst, argues that the Republicans' success in portraying Iraq as part of a wider war on terror may actually hurt them, because “failures in Iraq could cause Americans to see the war on terror as failing as well.”

In Britain, too, public opinion has hardened in favour of pulling out the 7,200 British troops that are based mainly in the Shia south of the country, ever since the remarks of Britain's top general, Sir Richard Dannatt, that their presence might be “exacerbating” security problems. An ICM poll for the *Guardian* this week found that over 60% of Britons want the troops brought home this year, regardless of the consequences for Iraq. Despite the urging of Iraq's deputy prime minister, Barham Salih, during a visit to

London this week that Britain and America should not “cut and run”, Margaret Beckett, the foreign secretary, conceded to the BBC that future historians might come to judge the invasion as “a foreign-policy disaster”.

Certainly the news from Baghdad is almost uniformly bad. Nearly 90 American soldiers, sailors and marines have been killed in October so far, the highest monthly total this year. At least 300 Iraqi soldiers have also died in roughly the same time period. The Iraqi civilian death toll, far more numerous but also harder to count, appears to have climbed as well. One American spokesman reports a “disheartening” 22% surge in violence in Baghdad, despite a three-month-long American campaign to suppress sectarian killing in the capital.

This month also witnessed the eruption of a simmering conflict between rival Shia militias in the south, as fighters from the radical Mahdi Army seized control of much of the town of Amara, the capital of the Maysan governorate. The southern battles are especially distressing to the British, who had hoped to turn Maysan—one of two provinces in the south where British forces still bear primary responsibility for security—over to Iraqi control within months.

Of the two main threats to security, coalition officials say that Shia militia violence is now a bigger problem than the Sunni insurgency. The Mahdi Army, in particular, is thought to be responsible for most of the killing around Baghdad, which in turn—according to American officers—accounts for some 90% of the violence nationwide. But reports suggest that the “army” has splintered into groups as small as a few dozen individuals who frequently behave more like street gangs than religious zealots: kidnapping for profit, taking over petrol stations, murdering anyone who transgresses their puritan moral code, and generally using the movement's reputation for pious militancy to give themselves legitimacy.

Splintering Shias, confident Sunnis

Amara illustrates how hard it is to contain these networks. The origin of last week's clashes lies in the rivalry between the Mahdi Army and another Shia militia, the Badr Brigades belonging to the Supreme Council for Islamic Revolution in Iraq (SCIRI), a party which is strong throughout the south of the country. Although probably more numerous on the ground, the Sadrists tend to leave SCIRI in charge of provincial councils and police forces. As both groups allegedly dabble in oil-smuggling, abductions and other local moneymaking schemes, plenty of conflicts of interest arise.

The fighting in Amara reportedly began after a high-ranking Badr-affiliated police officer was killed by a roadside bomb and police, in response, arrested the young brother of the Mahdi Army's local commander. The Mahdi Army then swarmed into town and overran several police stations, levelling them with explosives. At this point the state sent in extra troops, while British forces in the area provided back-up. The Iraqi interior minister brokered a ceasefire with deputies of Muqtada al-Sadr, the Shia cleric who leads the Mahdi Army, but the potential for violence remains. And it is clear that, although the government depends on Mr Sadr to control his movement, he cannot stop the low-level day-to-day routine of sectarian killing in Iraq.

Some American commanders would like to take on the Mahdi Army properly, but feel they are being held back by Nuri al-Maliki, the prime minister. He has made them set free captured Mahdi Army leaders. Mr Maliki admits that he has blocked a big offensive in Sadr City, the crowded east Baghdad slum which is the militia's main support base, for fear of massive civilian casualties. He is in an awkward position; the Sadrists are one of the three main movements in his Shia coalition, and his government would probably not survive a massive uprising against it.

The Sunni Arab insurgency is also running in high gear. Multiple-fatality bombings, usually an insurgent rather than militia tactic, are more frequent than ever, with more than 50 every month from June to September (see chart). The Americans continue to try to court tribal leaders in Sunni provincial towns, hoping to isolate al-Qaeda and other radical groups. But the heartland of Sunni militancy around the provincial capital of Ramadi remains as intractable as ever.

In mid-September a gathering of Ramadi notables declared that they were sick of the vicious puritans turning their town into a battlefield, and vowed to drive the radicals out. A month later,

however, truckloads of masked militants from the Mujahideen Shura Council, an al-Qaeda-dominated umbrella group, staged a daylight parade throughout the city, suggesting that the guerrillas are as confident in their control of Ramadi as ever.

The marchers in Ramadi were calling not just for the ejection of the Americans from Iraq, but for the creation of a separate Islamic emirate. Other recent militant statements have defined this state as comprising only the Sunni heartland—parts of Baghdad, together with the provinces of Anbar, Diyala, Kirkuk, Salaheddin, Nineveh and parts of Babil and Wasit—as a reaction to Kurdish autonomy in the north and Shia demands for a federal south. Until recently, Sunnis have tended to leave calls for an Iraqi break-up to the Shia and the Kurds, denouncing partition proposals as an American-Israeli scheme to destroy the country. The militants may be adopting this position in order to pose as defenders of the Sunni population. But it is unlikely that either the United States or the new Iraqi government would tolerate an al-Qaeda-run mini-state in western Iraq.

The lone oasis of stability in Iraq remains the predominantly Kurdish north, now seeing an economic boom as Iraqi business relocates to its relative peace and security. Kurds there frequently grumble about corruption and administrative lethargy on the part of their government, formed by two rival former guerrilla movements, but still consider themselves fortunate compared with the rest of the country. They are particularly proud of their government's decision to bring in foreign companies, over Baghdad's objections, to explore local oilfields. This, they feel, may lay the groundwork for financial independence and secession.

The north may not be quite as tranquil next year, however. Kurdish leaders say that they are still on track for a December 2007 referendum in which the province of Kirkuk and other “disputed territories” will vote on whether they will join the Kurdistan autonomous region. Kurds now think that their compatriots and allies have enough of a majority to win the referendum, but the region is still occupied by hundreds of thousands of Sunni Arabs, Turkish-speakers and Shias, some of whom will strongly resist incorporation into Kurdistan.

Trying to hand over

In this maelstrom, what can the Americans do? Since this summer they have defined their military “main effort” as the build-up of the Iraqi army and police. Although the police have proved a disappointment, and are considered by many Sunnis to be little more than an arm of the militias, the army is a qualified success. Though plagued by poor discipline, inefficiency, corruption and desertion, it has so far remained politically reliable. And although not nimble or numerous enough to prevent low-level, day-to-day killings, it is probably now strong enough in most cities to prevent the militias and insurgents from simply taking over.

At an October 24th press conference America's top general in Iraq, George Casey, said that the job of building up Iraqi forces was about 75% done, and that they were about 12-18 months away from being able to assume full responsibility for security. He suggested also, however, that he might need a bigger American force in the meantime. George Bush, for his part, says that American forces will remain in Iraq for at least the remainder of his presidency, until “the job is done”.

In Britain, too, there is still surprisingly little deviation among ministers from the official line that the Iraqi army should be given at least another 18 months to increase its capacity to deal with the insurgency and the warring militias. British ministers are most worried that the political pressures on Mr Bush may force him to withdraw American forces prematurely, leaving the alliance humiliated. Tony Blair has hinted at a slower retreat, saying British troop numbers may be cut by half within a year.

The political “main effort”, meanwhile, lies in persuading the Iraqi government to reach out to its Sunni compatriots, in the hope that they may take action to reduce support for the insurgency. Zalmay Khalilzad, America's ambassador in Iraq, said on October 24th that the Iraqis had now laid out a “timetable” for key decisions: devising a system to share Iraq's oil wealth, amending the constitution, changing the agency in charge of purging former members of the ruling Baath Party into a body focused on reconciliation, and disbanding the militias.

The Americans mean to keep them to it. On October 22nd the *New York Times* reported that the administration was “drafting a timetable for the Iraqi government to address sectarian divisions and assume a larger role in securing the country”. Failure to abide by this, the *Times* said, would prompt America to consider “changes in military strategy and other penalties”.

Tony Snow, the White House spokesman, said this was not accurate. “There is still a very large to-do list before Iraq is in a position to sustain, [govern] and defend itself,” he said. “Are we issuing ultimatums? No.” He added: “We're working collaboratively with them.” On October 25th Mr Maliki indignantly denied that he was taking orders from anyone.

At an impressively substantial and forceful press conference on the same day, Mr Bush praised Mr Maliki, reminding his listeners that he had been in office for less than five months. America's patience was not unlimited, he admitted; but he promised that he would not put more pressure on the Iraqi government than it could bear. And he repeated that if he did not believe Iraq capable of defending, sustaining and governing itself, if he did not believe America could still “win”, “I'd pull the troops out tomorrow.” Neither he, nor anyone else, has much idea what to do if the politicians no longer have influence over the violence on the ground.

What would Democrats do?

No big changes are likely to be announced before the mid-term elections, but the president has said he will listen to the recommendations of the Iraq Study Group, a bipartisan commission appointed by Congress to study alternatives to current policy, which will issue a report, probably later this year. The group is led by James Baker, who was secretary of state under Mr Bush's father, and who says that “nothing” is off the table. The group is reportedly considering options such as a gradual pull-out of American troops and a diplomatic push to persuade Iran and Syria to curb the insurgent groups they are thought to encourage. They may also talk to any insurgent group, al-Qaeda apart.

If the Democrats capture one or both arms of Congress—as polls suggest is likely—they will have the power, in theory, to force a withdrawal of American troops by denying Mr Bush the funds to keep them in Iraq. Leading Democrats insist they will not do anything so drastic. But it is unclear what they will do, besides launching investigations into how Mr Bush and his crew handled pre-war intelligence and post-war rebuilding contracts.

If the Democrats ever agree on a strategy for Iraq, it will not be until after the election, because only then will they know which of them is in charge. Will it be Nancy Pelosi, the likely speaker if the Democrats capture the House of Representatives? Or Harry Reid, the probable majority leader if they win the Senate? Either would have to decide whether merely to obstruct the president's Iraq policy, or to work with him to improve it.

Several Democrats think the only way to make the Iraqi government take responsibility for its own defence is to set a timetable for pulling out American troops. Carl Levin, the top Democrat on the Senate Armed Services Committee, wants a “phased withdrawal” to begin by the end of the year, to “tell them

that they've got to take hold of their own nation".

Then again, such a plan might spur the militias to redouble their efforts at ethnic cleansing, so as to maximise the area they will control when the Americans leave. A study by the Brookings Institution, a think-tank, suggests that this is already happening, with hundreds of thousands of Iraqis having fled their homes since February because of "rumours and intimidation" and many more "teetering on the edge of displacement". Mr Baker says a sudden American pull-out would lead to "the biggest civil war you've ever seen".

Senator Joe Biden, the ranking Democrat on the Senate Foreign Relations Committee, argues that the only way to change course in Iraq is if Democrats and Republicans work together. Neither party will make the necessary tough decisions alone, he wrote in the *Wall Street Journal* this week, because neither wants to be blamed for what might happen next. Mr Biden has said he thinks some of his Republican colleagues are ready for a bipartisan approach to Iraq. But this seems unlikely until after the election. Some Republicans, meanwhile, are distancing themselves from the president. Lindsey Graham, a senator from South Carolina, told the Associated Press this week that Iraq was "on the verge of chaos" and added that the current plan was "not working".

One reason for the recent upsurge in violence in Iraq, argues Mr Bush, is that "the terrorists are trying to influence public opinion here in the United States" and "break our will". If so, it seems to be working. A Gallup poll this week found that only 19% of Americans think America is winning in Iraq. The popular Arab belief that Americans fervently covet their land could not be more wrong; on all sides, they long to be shot of Iraq. But there is no easy way out. A cartoon in the *San Diego Union-Tribune* captures the mood. A newscaster announces that "The US population has officially hit 300m people. In a poll, all but six of them agreed we need a new strategy in Iraq." Yes, but what?

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Politics in the mountain West

There's electoral gold in those hills

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Have the Democrats struck the mother lode in the Rockies?

TWO years ago the eight states of America's interior West were coloured in red. Unlike the leftish west coast, they had all voted for George Bush over John Kerry, often resoundingly so. In one of those states, Colorado, voters in the third district also elected John Salazar to the House of Representatives. Mr Salazar—a plain-spoken farmer who wears a cowboy hat and likes guns—seems in many ways a caricature of the homespun politicians who thrive in the western reaches of Mr Bush's Republican heartland.

Like Mr Bush, Mr Salazar favours low taxes, including a repeal of the estate tax. His district, like many parts of “red” America, is vast and thinly populated. Roughly the size of New York state or Greece, it sprawls down the western slope of the Rockies and across the southern part of the state through Pueblo. Mr Salazar got elected partly because he stuck up for farmers' and ranchers' water rights against the grasping city folk from Denver. Yet despite being rugged, rural and right-of-centre on many issues, Mr Salazar does not quite fit the mould of a red-state politician. For one thing, he is a Democrat.

Increasingly, he is not alone. Over the past few years other Democrats have also won prominent races in the heart of the interior West. They have taken over governors' mansions in four of the region's eight states (Arizona, New Mexico, Montana and Wyoming) since 2002. Bill Ritter in Colorado will soon become the fifth, if he hangs on to his strong lead in the race to succeed Bill Owens, a term-limited Republican. In 2004 Mr Salazar's younger brother, Ken, beat Pete Coors, a Republican beer magnate, to win one of Colorado's Senate seats. Another Senate seat could be forthcoming in Montana, where Jon Tester is leading against the three-term incumbent, Conrad Burns. And as the Democrats vie for control of the House this year, open seats in Arizona and Colorado are among their very best chances to make gains.

The Democrats have done this in many cases by being cultural claim-jumpers, expropriating the hearty rustic symbolism that Republicans consider their own. Both Mr Tester and Brian Schweitzer, the governor of Montana since 2004, are gun-lovers and farmers, like Mr Salazar. Mr Schweitzer takes his border collie to the office and boasts of its ability to herd cattle. Mr Tester makes frequent references to farm equipment. When a small group of doctors in Billings complained about malpractice suits recently (trial lawyers are huge donors to the Democrats), he replied that he knows more about greasing combines than medicine. Mr Salazar even says that Colorado Republicans are now trying to imitate him. “I do an ad on a horse, so my opponent has an ad on a horse,” he says.

Although many Democrats elsewhere do not approve of all those guns—or of Mr Ritter's anti-abortion stance—they could not be happier about the trend. Besides winning political races, these

westerners have been helping the national Democratic Party to shed its image as a bunch of effete urban intellectuals. Democrats love Mr Schweitzer, a blunt populist, not only because he hates free trade and expensive health care, but also because he talks tough to Republicans.

How the West might be won

Apart from making them seem folksier, can this trend offer the Democrats large and lasting gains? Populations are growing rapidly in many parts of the interior West, and many of the (legal) immigrants are unaffiliated voters from California and the Midwest. These newcomers could be potential Democratic voters in a region with growing political clout.

But Democrats will only make meaningful gains in the region if they stay to the centre on economics as well. The south-western states—Arizona, Nevada and New Mexico—are growing rapidly, but many newcomers are unaffiliated because they have a libertarian bent. Darcy Olsen, president of the Goldwater Institute, an Arizona think-tank promoting small-government conservatism, argues that people are moving to the south-west not just because it is sunny but also for its low taxes. Although Democrats are already competitive in all three states they will not get far if they bury voters in taxes and red tape.

Further north and east Utah, Idaho and Wyoming remain solidly conservative. Voters in all three backed Mr Bush heavily over Mr Kerry; all six of the states' senators and five of their six House members are Republicans. Montana is already pretty Democratic. Apart from Mr Tester's Senate bid and three presidential electoral votes, there is little more on offer.

The state to watch is Colorado, which has nine electoral votes. Over the past two decades the parties have tended to alternate in power at all levels: its two Senate seats are now split, and Democrats retook the state legislature in 2004. Voters' ideas have not changed much over that period: the parties just take turns letting them down. Republicans have done that recently by going to extremes on both social and tax issues. State legislators, for example, have been preoccupied with university professors' behaviour, cooling off periods for divorce and other sops to the right wing. The Christian right conducts increasingly vicious primary battles.

Colorado Republicans also went too far last year over a plan to tweak a 1992 initiative that limited spending growth. When many Republicans fiercely opposed the tweaking, even though voters clearly wanted to boost education spending, the party seemed out of touch. Some Republicans even suggested selling off the state house and other public buildings instead.

Can Democrats do better? A few of the party's patrons have been pouring in money to take advantage of the Republicans' over-reach, and the Democrats have been offering better candidates and running more organised campaigns. But Mr Salazar, for one, worries that if Mr Ritter wins the governor's race, Colorado Democrats will soon lurch too far to the left. If they do, guns and hats won't save them.

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Wind power in the Midwest

The answer, my friend?

Oct 26th 2006 | CHICAGO
From The Economist print edition

Can the windy Great Plains be a new power source, or is that just bluster?

BIOFUELS are not the only renewable energy sources that farmers in the Midwest get excited about. They are also keen to cash in on the strong winds that gust across the region. Five states—North and South Dakota, Minnesota, Iowa and Illinois—are among the nation's ten most reliably windy states, according to the National Renewable Energy Laboratory in Colorado.

Unsurprisingly, therefore, farmers and their politicians have rushed to cash in, as well as to pick up any subsidies that might be on offer. Minnesota is furthest along. It has already told electric utilities to generate 10% of their power from wind by 2015; its legislature is mulling a plan to double that target.

Wind farms are also sprouting up to the east. In rural Illinois Rod Blagojevich, the state's Democratic governor, has sung their praises as an environmentally friendly source of economic development. Across the region many farmers are either having wind turbines put on their land or are “wind prospecting” to gauge the breezes blowing over their fields. Many of these projects are small, however. And those in Illinois and Wisconsin draw on wind sources that are not as good as on the northern Great Plains. The best place to generate lots of reliable wind power is over a large area that straddles southern Minnesota, northern Iowa and the eastern Dakotas.

That area has a big drawback, however: hardly anyone lives there. To take advantage of those winds, the region would need some way to transmit the resulting electricity to big cities across the upper Midwest, such as Milwaukee and Chicago.

That would be expensive, says Dale Osborn of the Midwest Independent Transmission System Operator, which is charged with ensuring reliable power across the region. Mr Osborn reckons that the extra-high voltage transmission lines which would be needed to get wind power from the plains to the cities would cost roughly $2.3m a mile ($1.4m a km). Around 20% of that cost, he reckons, would go towards buying rights of way from farmers across Iowa and rural bits of other states. Land rights clearly are a problem.

Politics may also prove to be an obstacle. Why should you build transmission lines to tap better wind energy on the Great Plains, for instance, when you can instead help farm owners in your own state? “Illinois wants Illinois wind, and Wisconsin wants Wisconsin wind,” says Mr Osborn. “There is a lot of parochialism.”

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The armed forces and Iraq

The silent majority

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From The Economist print edition

Unhappiness with the war is growing within the military community

ON ANY Saturday San Antonio's colourful, lazy downtown is full of airmen. After graduating from basic training at nearby Lackland air-force base on Friday morning, they get a town pass. Last weekend the mood was quiet. Some airmen, Mum and Dad in tow, went for a ride on putt-putt boats. Others poked around the Alamo. One spent several minutes looking at a duck.

AP

Home at last

You can forgive the airmen for being subdued. As many potential soldiers have noticed, this is a difficult time to join up. The army has managed to scrape up slightly more than 80,000 recruits this year, but only by lowering its qualification standards and offering large enlistment bonuses. Next month it will introduce a new ad campaign, “Army Strong”.

The slogan can only do so much. After a particularly bad month the total number of dead American soldiers comes to roughly 2,800. The Defence Manpower Data Centre also counts more than 20,000 wounded and 30,000 who have sustained “non-hostile injuries”. Improved medical technology has helped thousands of soldiers survive injuries that would have been fatal in previous wars.

This is especially apparent in places like San Antonio where there are plenty of wounded veterans. The city is home to three air-force bases, an army post, and the Brooks Army Medical Centre. That facility specialises in burn victims, but in 2005, it opened the Army's second amputee centre. The first, Walter Reed Army Medical Centre in Washington, DC, had more than it could handle. As jarring as it is to see a young and otherwise healthy person missing several limbs, the terrible truth is that these cases no longer occasion much shock in San Antonio.

Things are hard on the home front as well. Extended deployments are so routine that the Maine National Guard provides life-size cardboard “Flat Daddies” and “Flat Mommies” for children with a parent in Iraq or Afghanistan. “I prop him up in a chair, or sometimes put him on the couch and cover him up with a blanket,” one spouse reportedly said. “I've tricked several people by that.”

In public at least bravado carries the day. Troops based at Fort Sam Houston, which is also in San Antonio, describe their recent tours in Iraq and Afghanistan as “fun”. During times when an ordinary guy might feel afraid “a sort of a rush kicks in”. One soldier allows that, after returning from Iraq, he mistook a late-night noise for a bomb. “Did you have trouble sleeping after you got back?” he asks his friend. “One night I woke up reaching for my weapon,” says the other. They shrug.

“For military families, and especially young service members, there's a lot of frustration about how long and how difficult this war has been,” says Jim Martin, a retired army colonel at Bryn Mawr College. But the magnitude of that frustration is hard to measure. “There are all sorts of laws pertaining to this,” says Richard Kohn of the University of North Carolina. “If you're on active-duty in the military, you're not going to be politically active beyond voting.” Active-duty officers, for example, are not allowed to criticise Mr Bush. The Uniform Code of Military Justice lays down that an officer who has “contemptuous words” for the president can be court-martialled.

Retired officers can say what they want, and a number have done so. But many are still reluctant to be openly critical of the war or its management. “There are conflicting currents in the military,” says Mr Kohn. Many veterans, he says, feel a sense of loyalty to the commander-in-chief and believe that support for the war boosts morale and cohesion among the troops. “At the same time,” he continues, “there was always some doubt about the necessity and appropriateness of the war [in Iraq] as a part of the larger so-called war against terrorism.”

The Dems of War

Some of the loudest doubters are currently running for office—as Democrats. James Webb, a former secretary of the navy, is up for the Senate in Virginia. Tammy Duckworth, an army pilot who lost both her legs in Iraq, is hoping to represent an Illinois district in the House. Jay Fawcett, a retired air-force lieutenant-colonel, is running for Congress from Colorado's fifth district. A recent poll showed him tied with the Republican, Doug Lamborn.

It helps Mr Fawcett that his foe is a bit of a buffoon. Mr Lamborn once campaigned to swap the names of Mount Democrat and Republican Mountain because the former is taller. Still, the race is worth watching. Colorado Springs, a stronghold of the religious right, has two air-force bases, an army post and the air force academy. The district has been a Republican citadel since it was created in 1972. Mr Bush won it with two-thirds of the vote in 2004.

People who study the armed forces, including Mr Kohn and Mr Martin, agree that officers support the Republicans by a big margin. But having questioned many, Mr Kohn has found that their conservatism has its limits. Enlisted men and women still lean towards the Republican Party too, but not as heavily as they once did. George Marshall, the army's chief of staff during the second world war, once famously argued that soldiers should not vote because it might compromise their ability to serve. There may yet come a day when some Republican strategists are tempted to make that same argument.

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Maine's water wars

Source of trouble

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Is bottled water hurting aquifers?

HOWARD DEARBORN, an 88-year-old inventor, is worried about the pond beside his house. In the past few years, he says, a sandy bottom has given way to green gunk and his visitors refuse to swim in it anymore. That is not his only water worry. Recently, “the water table has dropped down so much that my pump was sucking air.”

Mr Dearborn believes, though he admits he cannot prove it, that his problems stem from the arrival in Fryeburg of Poland Spring, a Maine bottled-water company owned by Nestlé. Fryeburg, in south-west Maine near the New Hampshire border, sits on an enormous aquifer. It has caught the eye of the $10 billion bottled-water industry, which enjoyed 9.6% growth in per-capita consumption in America last year. Poland Spring, the top-selling spring-water brand in America, will this year pump about 110m gallons (24m litres) out of Fryeburg.

Locals have raised a fuss. So many people crowded into a recent town meeting on water that the discussion had to be postponed to find a larger venue. As well as the long-term effects on the aquifer, people worry about the traffic, which will get worse if the state superior court allows Poland Spring to build a bottling plant in Fryeburg. Emotions crystallised two years ago, when the town's water ran dry because of a pump failure, but Poland Spring's operations carried on.

Managers at Poland Spring fire back that their factories are good for a state whose manufacturing sector is languishing. Maine gets plenty of rain—up to 48 inches (19cm) on average in Fryeburg. “We take only what the aquifer can afford,” according to Tom Brennan of Poland Spring—which says it accounts for just 0.2% of Maine's groundwater use. As for the noise, Mr Brennan says that “our incremental addition to truck traffic is insignificant in the long run” since Fryeburg already sits on a big route from Portland to Canada.

The leaders of the Maine towns are keener. Last week officials in Kingfield, a small town in central Maine, unanimously approved construction of a water-bottling plant there (Poland Spring's third in the state). A few hundred million gallons of water will also be pumped out of the local aquifer each year.

But the battle will continue. Jim Wilfong, a former state legislator from the Fryeburg area, failed in his effort to get a punishing 20-cents-a-gallon tax on big water extractors (read: Poland Spring) onto the Maine ballot in November. But he is calling for a review of Maine's groundwater laws, which in effect allow landowners at the moment to pump as much as they wish. These are troubled waters indeed.

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The minimum wage

A blunt instrument

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A higher minimum wage may not kill many jobs, but won't help many poor people

IF THE mid-term elections have one central economic issue, it is higher minimum wages. Nancy Pelosi, the leading Democrat in the House of Representatives, has vowed that if her party wins control of that chamber on November 7th, she will introduce legislation to raise the federal minimum wage from $5.15 to $7.25 an hour within her first 100 hours as speaker. In six states, including the swing states of Ohio and Missouri, voters will also decide on whether to raise their state minimum wage. Democrats hope the presence of such initiatives on the ballot will lure their supporters to the polls.

Politically, the strategy makes sense. Americans are hugely in favour of raising minimum wages. In one recent poll 85% of respondents said they supported the idea. Over half said they would be more likely to vote for a candidate if they found out that he supported introducing a rise.

Advocates claim more than politics on their side. They argue that a higher minimum wage also makes economic sense. The Economic Policy Institute (EPI), a left-wing think-tank, recently published a letter signed by over 650 economists, including five Nobel prizewinners, which advocated a rise. Since the federal minimum wage was last raised in 1997 its real value has eroded dramatically. It is now less than in 1951 (see chart). Not only would a modest rise have "very little or no effect" on employment, the letter said, it would be an important tool in fighting poverty.

Strong stuff. But, laureates notwithstanding, it does not reflect a consensus among the dismal scientists. Overall, economists have become less worried about the job-destroying effects of a modest hike in the minimum wage. But most still reckon that it is at best a blunt instrument for fighting poverty.

The academic argument—and there has been plenty of it in recent years—has focused on the employment effects. Elementary economics would suggest that if you raise the cost of employing the lowest-skilled workers by increasing the minimum wage, employers will demand fewer of them. This used to be the consensus view. But a series of studies in the 1990s—including a famous analysis of fast-food restaurants in New Jersey and Pennsylvania by David Card at Berkeley and Alan Krueger of Princeton University—challenged that consensus, finding evidence that employment in fast-food restaurants actually rose after a minimum-wage hike. Other studies though, particularly those by David Neumark of the University of California at Irvine and William Wascher at the Federal Reserve, consistently found the opposite. Today's consensus, insofar as there is one, seems to be that raising minimum wages has minor negative effects at worst. Lawrence Katz, an economist at Harvard University and signatory of the EPI's letter, agrees that "most reasonably well-done estimates show small negative effects on employment among teenagers".

So the academic debate has shifted elsewhere, although the division between sceptics and advocates remains much the same. Mr Neumark, perhaps the leading sceptic about the minimum wage, has published several papers arguing that employers spend less on training their workers as their labour costs rise; that more students drop out of school, lured by fatter pay-packets; and that workers in their late twenties earn less if they were exposed to high minimum wages as teenagers. Other studies, however, do not find this.

Where most economists agree is that the higher minimum wage does not do much to relieve poverty. That is partly because many poor people would not gain (since they do not work); partly because some of the costs of higher minimum wages are shifted onto poor consumers; but mainly because many minimum-wage workers are not poor. Only 5% of the workforce—some 6.6m people—will gain directly from a rise in the minimum wage, and 30% of those are teenagers, many from families that are not poor. Supporters of an increase, though, argue that once you include the “spillover” effects on workers who earn just above the minimum wage (but whose wages would rise as a result), the income gains from a hike are concentrated among poor families.

Not surprisingly, studies that try directly to measure the distributional consequences reach divergent conclusions. Several studies of the 1990s find that higher minimum wages helped reduce poverty, albeit modestly. Mr Neumark, unsurprisingly perhaps, finds the opposite result. He claims that increased minimum wages actually increased slightly the number of families in poverty (presumably because these workers disproportionately lost their jobs while well-off teenagers got higher wages).

Either way a better tool exists for helping the working poor: the earned-income tax credit (EITC). This tax subsidy, a “negative income tax” that tops up the earnings of the low-paid, was introduced in the 1970s and has been expanded four times since. Its benefits are currently focused on families with children. Single men get little from the EITC. Some left-leaning economists argue that it is important both to raise the minimum wage and expand the EITC. But a big EITC expansion is politically hard (unlike raising the minimum wage, it involves spending taxpayers' money). So others support a higher minimum wage as a second-best solution. If it were up to the economists though, fatter tax subsidies would be top of the list for helping the working poor.

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California drilling

Taxing times

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The row over severance

“PROPOSITION 87 will move California towards energy independence, with cleaner fuels, wind and solar power,” declares Bill Clinton in the slick commercial now running nightly on Californians' TV screens. “America has to change, but you can lead the way. Do what you've always done: claim the future.”

But will the voters on November 7th heed the Clinton appeal? Or a similar one from Al Gore, not to mention Hollywood glitterati from Robert Redford to Julia Roberts? The idea of Proposition 87, one of 13 initiatives that have qualified for the ballot, is that the nation's oil companies should pay a “severance” tax, varying with the market price of oil, of between 1.5% and 6% on each barrel they extract from California's oilfields, on-shore and up to three miles off-shore. The tax is supposed to generate $4 billion within ten years, and would be used to finance the development of alternative fuels and to subsidise conservation. The oil companies, the proposition says, would not be allowed to pass the tax on to the consumer.

Cue outrage from Chevron and its fellow oil producers: the proposition will mean higher petrol prices anyway they say, because it will depress Californian production and so increase expensive imports (last year, California supplied 37% of its own oil demands, Alaska 21% and foreign imports 42%). It will mean, too, lower tax revenues for the state, because the severance tax would lower their income tax liability, and lower property taxes for local authorities, because the oil reserves would be deemed to be less valuable. Meanwhile, oil companies would end up paying the highest taxes in the nation on their Californian output, reducing their incentive to look for more. Put the sums together, say the companies (supported by a raft of academics and newspaper editorials), and the tax will be self-defeating.

Perhaps they protest too much (the companies have been enjoying record profits, after all). While Steve Bing, a film producer best known outside Hollywood as the father of Liz Hurley's love-child, has poured at least $40m into supporting Proposition 87, the oil companies have retaliated with over $70m—making this the most expensive ballot fight in California's history. As “Yes” campaigners point out, the oil industry pays severance taxes in Alaska and Texas. And California's independent Legislative Analyst's Office, says the fiscal downside is modest.

A better criticism is the clumsy drafting of the proposition: amazingly, it is unclear whether the various levels of tax would be applied at the margin or on a whole-barrel basis. A barrel of oil priced at $70 would yield a tax of $4.20 if a full 6% tax were applied; on the other hand, if the first $10 is untaxed, and the value from $10 to $25 is taxed at 1.5%, and so on up the scale, the final proceeds would be just $2.17.

The voters will doubtless not bother with such arithmetic. In a Democrat-dominated state, the Clinton-Gore message, chiming with the goal of reducing California's oil consumption by 25% in ten years, rings in tune with a culture of environmental activism. Moreover, no one disputes California's need for cleaner air. According to the Yes campaign, 95% of the 36m Californians live in areas that fail to meet air-quality standards.

Yet none of this guarantees defeat for the oil companies on polling day. Last July, approval for the proposition was at 52%, with just 31% against; by last month, the lead had narrowed to more or less evens. What is clear is that Arnold Schwarzenegger, despite positioning himself as an eco-friendly Republican-lite governor, has no intention of lending a meaty hand. As his office puts it, the governor is against new taxes—so “he opposes the initiative but supports its goals.”

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Philly cheese steaks

Whiz wit?

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A sandwich is the star of a lawsuit

CHICAGO is famous for its deep pan pizza. Maryland has crab cakes and Boston baked beans. New Orleans has gumbo, New England clam chowder and Buffalo its wings, but no American dish is as closely identified with its hometown as the Philly cheese steak. “Rocky” Balboa, Philly's favourite son as played by Sylvester Stallone, ate one while training against Apollo Creed back in 1976. It's so much part of the city that when *Men's Fitness* magazine named Philadelphia the fattest city in America in 2000, the cheese steak got hit with a lot of the blame.

The famous dish, usually served with onions on an Italian roll, is in the middle of a trademark infringement lawsuit. According to the complaint, Pat's King of Steaks claims Rick's Original Philly Steaks has been illegally trading on Pat's name, crown logo and trademarked phrases. The two eateries are owned by cousins, grandsons of Pat and Harry Olivieri, the famed sandwich's inventors. So much for Philadelphia being the city of brotherly love.

Scott Pollack, the lawyer for Pat's, said the obvious customer confusion is damaging, especially as his client is well-known both nationally and internationally. Although Rick's has been opened for two decades, Pat's only filed the suit last week, possibly because in April Rick's opened a seasonal shop at Citizens Bank Park, home to the Phillies baseball team. A few weeks later, Rick Olivieri, Rick's Steaks owner, allegedly made reference on TV to Pat's, which has been in business since the 1930s, and from which he is accused of implying descent for his own business.

Companies can have the same trademark name as long as they are in different geographic or product markets. This may not work for Rick's, as the restaurants are less than two miles apart. Rick's may well use the popular nominative fair-use argument. This defence means a person may use the trademark of another as a reference or as a comparison.

This is not the first Olivieri family feud. A dispute over ownership arose in the 1970s, but was eventually resolved with one side buying out the other. Over the years Pat's has had a few run-ins with other pretenders to the logoed crown. Trademarks, unlike patents, cannot be used to stop others from copying goods or services. Little wonder then there are thousands of cheese-steak restaurants in Philadelphia.

The Philly cheese steak is serious business. Ordering etiquette must be adhered to. Customers must state their preferred type of cheese and whether onions will or will not (“wit” or “witout”) be added. John Kerry, when campaigning for president in 2004 in Philadelphia, botched it badly, asking for Swiss cheese instead of the more traditional Cheez Whiz, a processed cheese spread. Even provolone or American cheese would have been better. George Bush ordered “Whiz wit” like a local.

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Obamamania

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Barack Obama is unlikely to get a better chance to run for president

FOR a technological dinosaur, the book-publishing industry is having a stellar political season. The bloggers may type the night away, but it is good old-fashioned book-writers who are driving the political debate.

And nobody more so than Barack Obama. The junior senator from Illinois has deftly used the publication of his new book—"The Audacity of Hope: Thoughts on Reclaiming the American Dream" (Crown)—to stir up a frenzy about a possible presidential run. In recent weeks, he had already made the covers of two big magazines—*Time* ("The next president") and *Men's Vogue*. Then on October 22nd he admitted that he had "thought about the possibility", and would make his final decision after the mid-terms. Since then it has been all Obama all the time.

This is bad news for lots of Democrats with less exotic names. Several pundits have pronounced the Democratic primary a two-horse race between Mr Obama and Hillary Clinton, which is overstating things. John Edwards is strong with the grassroots; Al Gore is a still-rumbling volcano. But Mr Obama, who is 45, has transformed the race, jumping over greybeards such as John Kerry and giving the Democratic Party its biggest shot of excitement for years.

Mr Obama's not-quite-declaration is especially bad news for Mrs Clinton. The junior senator for New York has spent the past six years—some would say nearly six decades—buffing her presidential credentials. She has supported the war in Iraq to prove that she is "tough enough", made nice with her Republican tormentors and hoovered up Democratic money. And now a mere greenhorn, who was marking law papers when she was co-running a "two-for-the-price-of-one" presidency, has shoved her out of the limelight.

What makes this all the more galling for the Clintonistas is that one of Mr Obama's most obvious advantages is that he is not Hillary. Mrs Clinton comes with a pantechnicon full of baggage. (What exactly has Bill been doing to amuse himself in New York these past few years, for example?) Mr Obama, by contrast, is fresh-faced and, so far as we know, baggage-free. Nor is he above offering a gentle reminder of what people disliked about Clintonworld. "When I was a kid I inhaled," he said bravely this week. "That was the point."

Mr Obama has no shortage of positive qualities. He is a superb public speaker—his address to the 2004 Democratic Convention turned him into a celebrity even before he was elected to the Senate—and bright with it. He is also black. It is hard to overestimate the extent to which many Americans would like to elect a black man—or at least one of Mr Obama's calibre. The product of a mixed marriage—his mother was “white as milk”, in his words, and his father, a Kenyan rather than an African-American, “black as pitch”—he is still black enough to dodge the “Oreo” slur. His father left his mother when he was two; he was brought up by his grandparents. Common, a rapper, has even devoted a line to him: “Why is Bush acting like he trying to get Osama? Why don't we impeach him and elect Obama?”

Mr Obama's rapid rise has inevitably provoked criticisms. One is that he is a young man in a hurry. He should take his turn in the queue—get a Senate chairmanship under his belt, and learn the ways of Washington. Such advice is either malign or misguided. The 2008 race is a once-in-a-lifetime opportunity—with the nominations open on both sides and the country desperate for a fresh face and a new direction. If he waits until 2012, he will have to take on an incumbent president; by 2016 he could well be yesterday's news. And a Senate record is a wasting asset. At best, you accumulate hostages to fortune in the form of controversial votes; at worst, you contract senators' disease, droning on about mark-up, earmarks, filibusters and cloture.

The second criticism has more substance: that Mr Obama is a lightweight. How would a man who has no foreign-policy or military background fare against John McCain, the Republican front-runner? And how would someone with no executive experience deal with Mitt Romney, a successful entrepreneur and Republican governor? Mr Obama's political philosophy is all about blurring boundaries where it is not pure waffle. Politics involves making difficult decisions, not dodging them.

Not just a pretty face

That said, Mr Obama is tougher than he seems. His rhetoric is as carefully calculated as it is well crafted. He knows that the presidential vote is the most personal vote Americans cast: people voted for John Kennedy (who was only 43 when he was elected) because of his stardust, not his record. He knows that Americans want a president who can get beyond the politics of division. And he knows that Americans are suckers for optimism. If Bill Clinton was the man from Hope, Mr Obama is the man with the audacity of hope.

And beneath all the rhetoric is a tough-as-nails professional. Mr Obama took on a crowded Democratic field in the 2004 Illinois Senate primary to capture 53% of the vote. He has delivered plenty of pork to Midwestern interests—including championing domestic ethanol production, to save the planet, while opposing the lifting of tariffs on cheaper Brazilian ethanol. This is not a man who is above raising doubts, albeit subtly, about Mr McCain's age or Mr Romney's pandering to the religious right.

In 1995 Colin Powell used the launch of his memoirs to explore a presidential bid. He sold 2.6m copies of the book, but got cold feet about running. Mr Powell's punishment is that he will go down in history not as America's first black president but as an enabler of a war he privately thought a mistake. The Democratic Party needs to think carefully about picking a charismatic neophyte over a more seasoned operator. But it looks as though Mr Obama will be there to give them the choice.

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Brazil's presidential election

Lula the political prizefighter

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AFP

After a nasty campaign, Brazil's president will have to seek consensus and reform

FOUR years ago Luiz Inácio Lula da Silva, the leader of the left-wing Workers' Party (PT), won election as Brazil's president by wooing centrist voters with the soft-focused slogan *Lulinha, Paz e Amor*. In a run-off ballot on Sunday October 29th he seems certain to win a second term—but after a campaign in which peace and love have been in shorter supply than snow in the Amazon.

Lula had been expected to win outright in the general election on October 1st. Instead, Geraldo Alckmin, until recently the governor of São Paulo, the biggest state, did unexpectedly well, winning 41.6% to Lula's 48.6% and forcing the run-off. Mr Alckmin was helped by a last-minute scandal of the kind that the Workers' Party has produced like popcorn in the past four years. This one involved party workers offering to pay 1.7m reais ($800m) for a dossier which smeared José Serra, Mr Alckmin's successor in São Paulo. But he also benefited from anger against the government in the south and centre-west, where drought and the strong real have hurt farming and some industries.

In a month of campaigning since then, Lula has widened his lead to 20 percentage points, if the polls are right. To repair relations with farmers, he recruited Blairo Maggi, newly re-elected as governor of the grain-growing state of Mato Grosso and himself the world's largest soyabean producer. He is courting the disgruntled middle class, which does not benefit from federal cash transfers to the poor—nor from those that go to the rich through high interest rates on government bonds. In debates, Lula has managed to make the PT's serial scandals sound almost like a virtue. “The time when things are swept under the carpet is over,” he declared.

Most of all, he found a way to turn the pro-business leanings of Mr Alckmin and his Party of Brazilian Social Democracy (PSDB) against them. Lula's predecessor as president, Fernando Henrique Cardoso, privatised electricity distribution, the telecoms monopoly and Companhia Vale do Rio Doce, a mining giant. Mr Alckmin has overseen São Paulo's own privatisation programme. Such is the PSDB's addiction to sell-offs, Lula suggested, that it would sell parked cars off the street.

Brazilians tend to forget the successful sell-off of telecoms, banks and many industries. They remember that electricity privatisation was rushed and incomplete, and followed by blackouts (most power-generation remained in state hands). Lula's scare tactic worked especially well with the 7% of voters who backed Heloísa Helena, a leftist expelled from the PT because of her opposition to pension reform. Many

who backed her as a protest against the PT's corruption now think it preferable to Mr Alckmin's supposed yen to privatise.

In response, Mr Alckmin copied Lula's habit of wearing silly hats. He donned a Banco do Brasil baseball cap to show that he had no intention of privatising the bank or any other state enterprises, whose logos were plastered on his jacket. This gesture summed up Mr Alckmin's mistakes over the past month. He should have defended privatisation or changed the subject. Instead, he allowed himself to be placed “on the defensive the entire time”, says Clifford Young of IPSOS, a polling firm.

The privatisation scare has embittered an already nasty campaign, which has featured claims that a “small elite” (the PSDB) is plotting to seize power through a “coup” if necessary against the “spawn of Goebbels” (the PT) clinging to it by any means. Mr Alckmin stupidly claimed that if Lula is re-elected his presidency will end before it begins (because he cannot run for a third term). More stupidly still, a minister responded by comparing Mr Alckmin to Augusto Pinochet, Chile's former dictator.

Most damagingly, all this stifled discussion of the issue that matters most: how to lift Brazil's growth rate. Many economists argue that the main culprit is the heavily indebted state, which takes nearly 40% of GDP in taxes, keeps interest rates high and imposes burdensome and capricious regulation on enterprise. Mr Alckmin seems to understand this. He calls for a “management shock” to public administration and cuts in “superfluous spending”.

One of Mr Alckmin's advisers, Yoshiaki Nakano, caused a stir by proposing a cut in government spending of 60 billion reais ($28 billion), as well as temporary exchange controls to make the real more competitive. The candidate himself disavowed that idea, and says almost nothing about how he would tame public spending. He “doesn't advance beyond slogans,” says Cláudio Couto, a political scientist at São Paulo's Catholic University.

At least Lula recently admitted the need to reform further the pension system for private-sector workers. Although Brazil is still a country of young people, this has a deficit equal to 2% of GDP. But he quickly added that workers should not have to pay more. By accusing Mr Alckmin of scheming to starve the state, he suggests he is happy to feed the glutton. Both candidates, who may in fact favour a healthy diet, pander to voters who do not. That makes it harder to cure Brazil's Stockholm syndrome, a love for a state that holds the economy hostage.

The president's men are now fretting that mudslinging and scandal may lead to a “third round”, with Lula formally re-elected but the opposition trying to subvert him, harassing the government for corruption and blocking legislation. That could happen: Lula's opponents may end up controlling the Senate. If he wins his second term, the president will have to move quickly to apply balm to the wounds he has opened. If not, he will have only himself to blame.

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Colombia's army

Under fire

Oct 26th 2006 | BOGOTÁ
From The Economist print edition

Bombings, real and otherwise

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AP

Uribe presses the generals for results

JUST a couple of weeks ago, Colombia seemed closer than it has been in years to seeing government negotiators sit down for face-to-face discussions with the FARC, the country's largest rebel army. Then a car bomb exploded at the army's War College in the heart of Bogotá. As well as injuring 23 people, it put paid to the chances of talks about swapping the hostages held by the FARC in jungle camps for imprisoned guerrillas. The FARC had mistaken his willingness to talk for weakness, said a visibly angry Álvaro Uribe, Colombia's conservative president. He ordered the army to try to rescue the hostages.

The bomb capped a bad few months for Colombia's army. Under Mr Uribe, the armed forces have had more manpower and resources. The president's "democratic security" policy has seen a sharp fall in killings and kidnappings. Opinion polls show that the army is one of Colombia's most respected institutions. But recent scandals have eroded its credibility.

These began in May when troops ambushed and killed ten members of a police drug squad. Investigators quickly discovered that far from being a tragic instance of "friendly fire", the killings were ordered by drug traffickers for whom the soldiers were working. In another drug-related incident, eight soldiers face criminal charges for killing six civilians in an operation presented as a kidnap rescue gone wrong.

Even more worrying are signs that the army may have responded to Mr Uribe's intense pressure for results by faking "successes". Troops from the army's Fourth Brigade are under investigation for the deaths of 29 civilians allegedly dressed in fatigues and presented as guerrillas killed in battle. At least two army officers are suspected of paying former guerrillas to stage fake bomb plots ahead of the start of Mr Uribe's second term in August, in order to allow the army to foil them. One of the bombs went off on July 31st, killing a civilian and wounding 21 people.

Though there are doubters, the bomb at the War College probably was the work of the FARC. After the blast, Mr Uribe acknowledged the suspicions, saying that such accusations should not create "a smokescreen for terrorist acts". The fact that the FARC was able to place a bomb at the place where officers learn to combat them on a day when the top army commander was there does not mean that Mr Uribe's security policy has failed, according to Román Ortiz, a political scientist at the University of the Andes. "It means that the task is not complete."

The United States has given Colombia more than $4 billion in aid since 2000, much of it to the army. Nicholas Burns, a senior State Department official, said this week during a visit to Bogotá that the administration will ask Congress to maintain aid at its current level of some $600m a year until 2008. But he also said he had raised concerns about corruption and abuses by the security forces.

According to Juan Manuel Santos, the defence minister, the scandals are "isolated" incidents that do not reflect the army as an institution. Nevertheless, he has launched a review of military recruitment, training and promotions. If Colombians are not to lose faith in their army, this better come up with some

changes.

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Venezuela

Death in El Dorado

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Gold miners clash with Hugo Chávez's revolution

Get article background

Reuters

SOMEWHERE beyond the imposing waterfalls that mark the meeting of the Caroní and Orinoco rivers lies a city paved with gold. At least that is what Sir Walter Raleigh, a 16th-century British adventurer, once believed. That mirage cost him his fortune, his son and, eventually, his head. In the centuries since, the dream of El Dorado has brought riches to a few and poverty, suffering and death to many more. Among the latest victims were six miners allegedly killed last month by Venezuelan soldiers who were enforcing a recent decree by the self-styled “socialist” government of President Hugo Chávez that bans mining in the Caroní basin.

Venezuela's vast south-eastern state of Bolívar is rich in gold and diamonds. But successive governments have failed to provide a legal framework that would encourage large-scale investment. Work at Las Cristinas, a huge gold deposit, has been halted by lack of legal permits. Meanwhile, tens of thousands of informal miners work smaller deposits in the area.

They are doing much environmental damage. They have destroyed parts of a once-pristine rainforest. They use high-pressure hoses, mounted on barges, to churn up the river bed. That silts up the river, which poses a threat to the world's second-biggest hydroelectric dam, downstream at Guri, which supplies more than half of the country's power.

Officials have offered the miners “retraining”. But their leaders say they have seen none of the promised compensation for giving up mining nor investment in alternative jobs. In La Paragua, a small riverport where the dead men and their families lived, the walls are covered with angry graffiti calling for an end to the army's policing of the area. Residents built burning barricades and torched the army checkpoint at La Paragua, which is some 200 kilometres (125 miles) west of the present-day town called El Dorado.

Officials at first said that the men had died in a “clash” between armed miners and the troops. But Manuel Felipe Lizardo, who survived after being shot twice and left for dead, told a different story. He says the troops split the miners into two groups, forced them to lie down and then murdered them. The brother of one of the victims said the dead men were not mining but packing up their equipment.

The soldiers had arrived in one of the Venezuelan army's brand-new Russian helicopters, bought earlier this year by Mr Chávez. Fourteen officers and men have been arrested in connection with the case. The government insists their superior officers were not involved, and that the anti-mining operation will continue.

The massacre was not an isolated incident. Another 18 soldiers are accused of “abuse of authority” in connection with an almost simultaneous case on the upper Caura river. Four men drowned there, allegedly when fleeing an army operation. Some survivors say they were deliberately burned and that the soldiers stole gold and diamonds. More recently, a Guyanese miner was shot dead on the border between the two countries. In La Paragua itself two men were killed by the army in March.

Rafael Madero, a local miners' leader, says the solution is to allow small-scale miners to stake legal claims. Geraldine Malasano, a lawyer and environmentalist who has lobbied for the miners but supports Mr Chávez's government, echoes official disdain for individual property rights. But if the government is to bring the goldrush under control, she says, it must take the miners' views into account. In Venezuela's south-east, El Dorado gleams more brightly than Mr Chávez's socialist revolution. “It's the dream of gold,” says Ms Malasano, “as it has been down the centuries.”

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Farming in Argentina

Biting the hand that feeds

Oct 26th 2006 | BUENOS AIRES
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Booming in spite of the government

AS SO often before in the past century and a half, Argentina's farmers have come to their country's rescue. In large part because of prescient investment made in the 1990s, farm products accounted for 80% of foreign-exchange earnings last year and paid export taxes equal to 6% of government revenue. Two products in particular, soyabeans and beef, have spearheaded Argentina's recovery from its economic collapse of 2001-02. But the farmers complain that an interfering government risks killing the golden goose.

Argentine farming commands formidable competitive advantages. Some of these are natural. The Pampas contain some of the world's best farmland, while the Paraná river provides low-cost transport. Others are entrepreneurial. Take soyabeans: in the 1990s, farmers were quick to innovate, adopting genetically modified seeds and no-till planting. Partly by allowing the use of cheaper, poorer land, such methods have cut average costs by half in a decade. Some $700m was invested in efficient, modern processing mills to turn soyabeans into flour and oil.

The investment was well-timed. Chinese and Indian demand for animal feed has boosted the price of soyabeans. According to Pablo Adreani of AgriPAC, a consultancy, a typical hectare's worth of soya costs around $300, and currently sells for about $625. The government takes a hefty 23.5% of soya revenues in export taxes—a total of $1.9 billion last year. Yet even after taxes, profit margins approach 40%. As a result, soya production has expanded by 57% over the last six years.

Beef farmers had high hopes of a similar bonanza. Although farmers have switched 7m hectares of land from cattle to soyabeans over the last decade, beef production still rose from 2.5m tonnes in 2001 to 3.1m tonnes in 2005. An outbreak of foot-and-mouth disease in Brazil last year disabled a competitor, allowing Argentine exports to win new markets.

But that in turn caused beef prices to rise at home (see chart). No Argentine meal is complete without meat, which accounts for 9.2% of the basket of goods used to track inflation. The government's expansionary policies caused inflation to rise to 12.3% last year. President Néstor Kirchner ordered “voluntary” price controls. He took particular aim at beef producers. After tripling the export tax on beef to 15%, in March he imposed a near-total ban on exports.

Farmers responded with a strike, briefly withholding their animals from Liniers, the vast cattle market in Buenos Aires. The export ban cut prices at Liniers by 30%. But butchers and supermarkets only cut theirs by about 7.5%, pocketing the difference. So the normally stubborn Mr Kirchner backtracked, allowing exports to reach about 65% of their 2005 level and offering beef producers subsidised credit and tax breaks to encourage them to increase output. If the price is not allowed to rise, this will not produce investment, says Victor Tonelli, a farmer and consultant.

The world is likely to continue to demand Argentine soyabeans and beef. That means the farmers will probably continue to invest. Mr Kirchner's bullying has caused some foreign utilities to pull out of Argentina. He knows that is not an option open to the farmers.

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South Korea and the North

Testing times

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North Korea's nuclear test leads to political confusion in the South

IT IS a place of mythical beauty—its peaks and pine forests the stuff of songs and scroll paintings—but Mount Kumgang, just on the northern side of the divided Korean peninsula, has become a symbol of all that is troubled about South Korea's policy towards its bad neighbour. Since 1998 the South has run a tourist resort at Mount Kumgang, which 1.4m South Koreans have visited. For Roh Moo-hyun, South Korea's president, this (along with a miserable light-industrial park at Kaesong) was proof that his strategy of engaging with North Korea, known as the “sunshine policy”, was bearing fruit. But since North Korea exploded a nuclear device on October 9th, if not before, the fruit has been foul.

The point of engaging North Korea was to coax Kim Jong Il and his regime to behave better. Engagement was supposed to bring economic benefits to the benighted North; a modicum of mutual trust was meant to lessen its threat. These assumptions were badly upset in July, when Mr Kim conducted missile tests; his nuclear test has blown them away. Mr Roh's administration, which has another year to run, is discredited, its popularity rating in the teens. This week both the defence minister and the minister for unification offered to resign.

Quite right too, say Mr Roh's opponents. In particular, the nuclear tests have stirred anger at the money given over several years to a foul regime: public and private money, above the table and under it. More thoughtful critics say the sunshine policy was originally a sensible one, meant to transform the North with a view to reunification. But engagement, particularly under Mr Roh, became an end in itself. Thereby, it can be argued, the policy changed the South more than the North.

How much money it has cost the South may never be known. At the government's urging, Hyundai, a family-held conglomerate, sent some $500m discreetly to Mr Kim to secure a historic summit in 2000 between the Dear Leader and the architect of the sunshine policy, the then president, Kim Dae-jung (no relation). The opposition Grand National Party (GNP) claims that, officially, some $1.2 billion of government cash has gone to North Korea since 1998 (not counting lashings of humanitarian aid, now temporarily suspended). The government disputes that figure but, amazingly, no full audit trail exists.

Among other things, the South Korean government has subsidised visits to Mount Kumgang. These subsidies, it promises, will now stop, but a big chunk of the revenues from the resort—the 40,000 visitors in a usual month pay up to $500 each—will continue to go straight into the regime's pocket. In all, Hyundai, which built the resort and runs it, has sent $850m in royalties to Mr Kim and his cronies.

America's secretary of state, Condoleezza Rice, and its envoy for North Korea, Christopher Hill, who

visited South Korea last week, are critical of the Mount Kumgang resort, which they believe generates cash for weapons of mass destruction. In addition, in talks this week over a proposed free-trade agreement between South Korea and the United States, American negotiators made it plain that imports from North Korea through the Kaesong zone could play no part in such a deal—thereby undermining the zone's rationale. The GNP has criticised both projects.

Yet Mr Roh and the ruling Uri party continue to defend them. They are, after all, the only fruits of engagement. During Ms Rice's visit, Ban Ki-moon, South Korea's foreign minister, who will soon become secretary-general of the United Nations, emphasised the “positive aspects” of the industrial park, as well as the “symbolic” importance of Kumgang in reconciling the two Koreas. The Uri party's chairman, Kim Geun-tae, goes further, claiming the Kumgang tours are needed more than ever.

Though Mr Roh's government has given its approval to stiff American-led sanctions against North Korea, which were passed by the UN Security Council on October 14th, it in fact shows little appetite for confrontation. That is partly because many South Koreans share a blind faith in the ultimate benign nature of the North's brutal regime—about which they are remarkably ill-informed. On October 25th North Korea said the South's participation in the sanctions would be a “declaration of confrontation” for which it would pay “a high price”.

Most Southerners think the North's crude nuclear capability does not represent a big new threat to them. North Korean artillery, after all, has long been positioned within range of Seoul's northern suburbs. Meanwhile, South Korea's predominant political consensus, says Andrei Lankov of Kookmin University in Seoul, is to seek gradual change north of the border in ways that might eventually narrow the vast income gap between the two sides. Tightening the screws too far risks goading Mr Kim to strike back. A collapse of the regime, followed by reunification, would impose unbearable costs on the South. Even the opposition GNP, says Park Jin, a member of the party, believes in maintaining dialogue with the North, while adding some pressure.

It is a path that is likely to lead South Korea increasingly into conflict with America, which wants stiffer confrontation with the North. In annual bilateral defence talks last week in Washington, DC, America's secretary of defence, Donald Rumsfeld, pressed South Korea to join the American-led Proliferation Security Initiative, which is designed to interdict ships carrying material for weapons of mass destruction. The South Korean government is vacillating, fearing that this would rile the North and so increase the nuclear threat.

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China's water supply

A modest proposal

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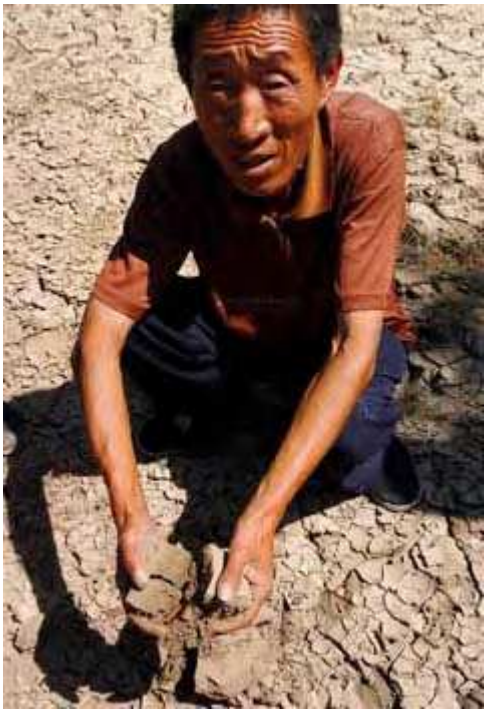
China should liberalise water pricing

HOW to provide sufficient clean water to the vast and arid north of China has long been a headache for its rulers. Of late they have considered some ambitious proposals. One of the most hotly debated, to divert water hundreds of kilometres from Tibet at a cost of tens of billions of dollars, was scorned this week by the water minister. What about a more modest (and less Maoist) approach: using market-driven prices to deter waste and pollution?

Market solutions do not come naturally to Chinese officials. For the past four years two huge diversion projects have been under way to bring water from the Yangzi River basin to northern China. Work on a more technologically challenging third route, involving blasting through mountains to link the Yangzi's upper reaches to the Yellow River, is expected to begin around 2010. The proposal castigated by the water minister, Wang Shucheng, on October 24th was even more grandiose. It would extend the link to the Yalu Zangbu river, as the upper reaches of India's Brahmaputra river are known in China. Mr Wang described this as “unnecessary, unfeasible and unscientific” (while stressing that this was his “academic” opinion). India must be relieved.

AP



Crumbling to dust

Meanwhile, China has been reluctant to impose tougher penalties on water polluters or higher tariffs on consumers. It fears that higher prices would drive industries away from the north and make it more difficult for struggling state-owned enterprises to turn a profit. It also worries about angering household consumers, particularly in the countryside. According to a government survey, water prices in 36 big cities have risen an average of 10% annually for the past three years (Beijing's have risen 30-fold in the past 14 years). But in August a government think-tank said prices remained only about a third of the world average. It called for price reforms to be speeded up. On October 20th Beijing published a five-year plan for economic and bureaucratic reforms in the capital. This called for water prices to reflect supply and the cost of delivery by 2010. The national government said earlier this year that it aimed to cut water consumption per unit of GDP by 30% in the same period.

Frank Gong, of J.P. Morgan Securities, says a resolution issued by the ruling Communist Party this month on building a “harmonious society” could help efforts to raise prices of water, as well as of heavily-subsidised electricity and fuel to market-oriented levels. The resolution mentions the need to “perfect” pricing and tax policies in order to help protect the environment. Always wary of causing social unrest, however, officials stress that any price rises will be “gradual”.

More money would help to fix leaking pipes (the Chinese media say urban pipes leak water at twice the rate of those in developed countries) and build more wastewater-treatment plants (at the end of 2005, around 40% of cities had no such facilities). Ma Jun, a water-conservation activist in Beijing, says many plants are underused or left idle because local authorities begrudge the cost of running them. Cities have been introducing sewage-treatment levies on household and industrial users in recent years, but the fees are insufficient to cover costs.

Raising prices does not mean that the water industry itself, a monopoly controlled by local governments,

has more incentive to operate efficiently. Although the government often talks of making decision-making more open, very little information is provided about how water rates are fixed. Since 2001 the government has required that public hearings be held before the raising of prices for necessities such as water and electricity. But these hearings have been stage-managed affairs. Mr Ma says the public would be more willing to accept water-price increases if the industry were more accountable.

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Investing in India

Sino things to come?

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Not all investors are equally welcome

DESPITE growing business and trade links, India and China are not friends. India, which lost a short war with China in 1962 over a territorial dispute that has not been resolved, still sees its huge neighbour as a strategic threat. This makes it anxious about any influx of Chinese workers or investment that might have security implications. So anxious, indeed, that it is considering formalising its existing unwritten controls on investment from China and other countries.

Among the measures being considered by India's National Security Council, which has been charged with drafting a National Security Exception Act, is a plan to subject proposed investments from, perhaps, China, Taiwan, Pakistan, North Korea and Middle Eastern countries to special examination. Scrutiny would also be paid to investments from tax havens like Mauritius, which is an important conduit for foreign direct investment in India and does not always reveal investors' details. Pranab Mukherjee, who was this week appointed foreign minister, can expect some diplomatic heat from these plans.

India's economic ministries are keen to make consistent what is currently a muddled regime of ad hoc controls. They are encouraged by the low level of investment from the countries concerned. But officials fear the restrictions could curb the growth in foreign investment, which is expected almost to double this year, to reach $12 billion. Businessmen hope the controls will at least be plainly advertised.

That might help one of the first Chinese companies to feel the squeeze, Huawei Technologies, a Shenzhen-based telecom-equipment company that has a six-year-old software centre in Bangalore employing 1,150 Indian engineers and 50 Chinese, plus a marketing company in Delhi. In 2001 it was accused of working for Pakistan and the then Taliban regime in Afghanistan (which it denied). Its bids for big government-controlled telecommunications-equipment contracts have been blocked, along with a trading-licence application, though the company believes it has found a way through the regulations. Other telecoms and airport-equipment companies—among a total of 50 Chinese businesses in India—have also run into snags, including difficulties in obtaining visas for visiting staff. It has taken Reliance Industries, one of India's largest groups, several weeks to persuade the government to issue visas to 1,800 engineers from Chinese Petroleum whom it wants to hire to lay a gas pipeline.

Three foreign port operators, including Hong Kong-based Hutchison Port Holdings, have recently been banned for security reasons from tendering for big container-port projects. The Hutchison decision was taken because of links between Li Ka-shing, who controls the group, and China's government. Yet a substantial share of India's mobile-phone market is operated by Hutchison Telecommunications, another Li Ka-shing company, which has never been censured because of links to China; but Orascom, an Egyptian firm, was scrutinised after it bought a 19.3% stake in Hutchison last December.

With trade between India and China expected to reach $20 billion this year, China will hope for signs of friendship from India when Hu Jintao, its president, visits Delhi next month. Its ambassador there, Sun Yuxi, complains of “unequal treatment” of Chinese companies. He says they should have the same opportunities as 150 Indian companies enjoy in China.

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Australia and the island-states

Pinch that minister!

Oct 26th 2006 | SUVA
From The Economist print edition

Weary of neighbouring politicians, Australia arrests one

Get article background

JOHN HOWARD, Australia's prime minister, flew into Fiji this week expressing the hope that the “balmy breezes of the Pacific” would calm tempers at a meeting of the Pacific Islands Forum. A few days earlier Australian police serving in a regional peacekeeping force in the Solomon Islands forcibly searched the office of the prime minister, Manasseh Sogavare, and arrested his immigration minister. Australia had also barred Sir Michael Somare, prime minister of Papua New Guinea, another chaotic neighbour it has been trying to put straight. The regional meeting was fiery.

Sir Michael accused Australia, once his country's colonial master and now training its officials, of bullying. Mr Sogavare presented a five-point plan to reduce Australia's part in the Regional Assistance Mission to the Solomon Islands, which has been trying to put a lid on ethnic unrest since 2003.

Bridling at overbearing Australia is nothing new for local leaders. Their citizens mind less: Australia has spent A$800m ($610m) on security and development in the Solomon Islands in the past three years and $300m a year on PNG. Yet Australia's diplomacy has perhaps been too muscular of late.

Trouble began last month when Mr Sogavare expelled Australia's high commissioner, Patrick Cole, having previously accused Australian police of stoking riots in April. Mr Sogavare also appointed a Fijian lawyer and Australian citizen with a spotted past, called Julian Moti, as his attorney-general.

Australia had Mr Moti arrested in PNG while he was travelling to the Solomon Islands, for allegedly raping a 13-year-old girl in Vanuatu in 1997. But before he could be extradited to Australia, Mr Moti was released and flown by a PNG military plane to the Solomons. Australian police arrested him there for having entered the country illegally.

When the government then claimed to have approved Mr Moti's entry, Australia arrested the minister and raided Mr Sogavare's office for evidence of the approval. The regional mission had keen support from Solomon islanders, but Australian strong-arming could undermine it. In a compromise deal, the leaders gathered in Fiji agreed to subject the mission to an independent review.

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Bangladesh

Isn't democracy wonderful?

Oct 26th 2006 | DHAKA
From The Economist print edition

An interim government in chaos

Get article background

ON OCTOBER 27th, after five years in power, a coalition of the Bangladesh Nationalist Party (BNP) and its Islamist allies was due to give way to what is supposed to be a neutral caretaker government. This body is meant to oversee elections due next January, meaning that for three months the two politicians who have taken turns to rule Bangladesh since the early 1990s, the outgoing prime minister Khaleda Zia, the BNP's leader, and Sheikh Hasina Wajed of the opposition Awami League (AL), will have no say in affairs of state. That is an arrangement many Bangladeshis would like to see endure.

But Bangladesh's constitution does not limit prime-ministerial terms, so another "battle of the begums" is in store. This round, the fourth since 1991, looks set to be the most severe test for Bangladesh's democracy since the country rid itself of a military dictator, Hossain Mohammad Ershad, in 1990. Rivalry between the two main parties is violent and little checked.

AP

Staving off defeat

It would help if the new government had an accepted leader. Days before it was due to take power, the main parties broke off talks over who should head both it and the country's election commission. The AL has threatened to call strikes if the country's president does what the constitution says he must, by appointing the previous chief justice, K.M. Hasan, to lead the interim government. It says Mr Hasan is a BNP supporter under whom fair elections will be impossible. Unless he is replaced by a neutral, it threatens to boycott the poll. As has happened lamentably often in Bangladesh, democratic dialogue may now give way to the politics of the street.

If the past is any guide, many people will be killed in mob violence and targeted assassinations. The AL admits that it has distributed staves among its followers for impending battles with BNP supporters. Bangladesh's politicians have been buying up bullet-proof vests in recent weeks, according to *Bangla Patrika*, a Bengali-language newspaper. Many observers fear the army may step in.

Until the end of last year it had seemed that Islamic militancy was the main threat to Bangladesh. A year ago a militant group called the Jamatul Mujahideen Bangladesh launched a series of suicide attacks on government offices and law courts. But the coalition government clamped down on the Islamists more firmly than many had predicted. A more mundane spectre, Bangladesh's intensely politicised judiciary, is now a bigger threat to the country's fragile democracy.

Lawyers complain of politically appointed judges at every level and direct government meddling in the lower judiciary. The BNP-led government—like the AL when it was in power—ignored a ruling from the Supreme Court that the judiciary must be made independent. A partisan caretaker government is the result. And indeed the AL has reason to feel victimised. A grenade attack on one of its rallies, in August 2004, nearly killed Sheikh Hasina and left other senior leaders dead or injured; it has not been properly investigated.

It is unclear whether an effective interim government can be formed or decent elections held—always

assuming there is no army coup. But, for a welcome change in Bangladesh, the impoverished country's demography does at least offer hope. In this election, for the first time in Bangladesh, seasoned voters with a firm allegiance to one of the two main parties will be outnumbered by voters aged between 18 and 35. This, and general disenchantment with the two main parties, explain why over 50% of voters are still undecided. One party could emerge from the scrimmage with a decisive victory.

That might explain why Muhammad Yunus, a Bangladeshi development economist and this year's Nobel peace prize winner, has suggested that he will launch a political party, creating a third force in the corrupt and chaotic land. Whether he will actually embark on this potentially suicidal plan is also unclear.

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Thailand

More unhappy Muslims

Oct 26th 2006 | TAK BAI
From The Economist print edition

The new government seeks new ways to pacify the violent south

THERE is no monument in the southern Thai village of Tak Bai to the dozens of protesters slaughtered by the government on October 25th 2004. On the second anniversary of the killing, Tak Bai's streets were quiet and there were few army or police patrols to be seen. Have the locals forgotten this outrage, the worst bloodshed since the insurgency in Thailand's Muslim south mysteriously reignited earlier the same year? No, says an anxious fishmonger at the village market: it is just that people are afraid even to talk about it.

The Tak Bai killings, and the southern unrest as a whole, are puzzles for which there are more questions than answers. It is unclear why the arrest of six village guards, accused of passing their weapons to separatist militants, stirred a huge protest, involving perhaps 1,500 people. The response of the security forces was vicious even by their ugly standards. First, troops opened fire on the mob, killing at least six (locals say more). Then they crammed hundreds of protesters into trucks, causing 78 to die, mostly of suffocation, as they were driven to a distant army barracks.

Two years later, it is unclear who is behind the almost daily rounds of bombings and shootings of soldiers, police, monks, teachers and other Buddhist civilians that plague southern Thailand. Security experts list Muslim separatist groups—some long-established, others whose existence is moot. Many say the violence is orchestrated by drug lords and other criminals, or by Thai politicians and the security forces themselves. Abdulrahman Abdulsamad, a local Muslim leader, says a mixture of all these factors is most likely to blame.

Violence has flickered in the south ever since Thailand annexed the region, which was formerly an independent sultanate, in 1902 and began trying to assimilate its mainly Malay-speaking Muslim people into a Thai-speaking, Buddhist nation. In the past three years, more than 1,700 have been killed by suspected militants, the security forces and unknown assailants. Three days before this week's anniversary, a soldier was killed by a bomb as he guarded monks begging for alms in Narathiwat city, the capital of the province in which Tak Bai is situated. Four days later, gunmen opened fire outside a mosque in a nearby village, killing an imam.

Earlier this year, Thaksin Shinawatra, the then prime minister, gave the army commander, Sonthi

Boonyaratglin, “full authority” to quell the unrest. But General Sonthi, a rare Thai Muslim in a senior post, wanted to negotiate with the rebels; Mr Thaksin did not. This may have been one reason for the coup that the army chief led last month. Surayud Chulanont, a retired general and now interim prime minister, promises a softer approach to the conflict.

In the past week he has toured neighbouring countries, seeking advice on the conflict. In Jakarta, Mr Surayud said the peace process under way in Indonesia's breakaway Aceh province would serve as a model. In Kuala Lumpur, he won promises of co-operation from Abdullah Badawi, the prime minister of Malaysia, which Mr Thaksin used to accuse of sheltering militant leaders. It was revealed that Mr Badawi's predecessor, Mahathir Mohamad, had been brokering secret talks between Thai officials and southern separatists even before Mr Thaksin's downfall.

Not long before the current spate of violence, Mr Thaksin abolished the civilian-led agency that oversaw the southern provinces. It had been credited with improving relations between the government, the security forces and local Muslims, especially by trying to root out many corrupt and brutal local soldiers and police. Mr Thaksin believed this agency had outlived its purpose; the new government is reviving it. Mr Abdulrahman, the Muslim leader, says he is encouraged by this and by the military government's appointment of Muslims to various jobs. He wonders, however, whether a serious peace deal is possible, given the uncertainty over who is actually behind the attacks.

Whether or not peace talks can get anywhere, the government could do much more to soothe southerners' fear and mistrust. Francesca Lawe-Davies of the International Crisis Group, a think-tank, notes that no police or army personnel have been prosecuted over the Tak Bai killings, while many of the protesters are still detained, two years later, over minor accusations. Many southerners might accept autonomy instead of independence if they felt they had a modicum of justice.

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China in Africa

Never too late to scramble

Oct 26th 2006 | BEIJING, LAGOS AND LUSAKA
From The Economist print edition

China is rapidly buying up Africa's oil, metals and farm produce. That fuels China's surging economic growth, but how good is it for Africa?

AFP

IN HIS office in Lusaka, Zambia's capital, Xu Jianxue sits between a portrait of Mao Zedong and a Chinese calendar. His civil-engineering and construction business has been doing well and, with the help of his four brothers, he has also invested in a coal mine. He is bullish about doing business in Zambia: "It is a virgin territory," he says, with few products made locally and little competition. He is now thinking of expanding into Angola and Congo next door. When he came in 1991, only 300 Chinese lived in Zambia. Now he guesses there are 3,000.

Mr Xu reflects just a tiny part of China's new interest in Africa. This year alone many bigger names than his have come visiting. Li Zhaoxing, China's foreign minister, swept through west Africa in January; President Hu Jintao visited Nigeria, Morocco and Kenya in April; and the prime minister, Wen Jiabao, knocked off seven countries in June. In the first week of November Chinese and more than 30 African leaders will gather at the first Sino-African summit in Beijing. And Chinese companies, most of them owned by the state, have been marching in the footsteps of their political leaders. But is this all good for Africa? Is it bringing the trade and investment that Africa so badly needs, or just meddling and exploitation?

The summit in Beijing is being greeted by Chinese officials and the country's state-run media with an effusion reminiscent of the cold-war era, when China cosied up to African countries as a way of demonstrating solidarity against (Western) colonialism and of outdoing its ideological rival, the Soviet Union. It supported African liberation movements in the 1950s and 1960s, and later built railways for the newly independent countries, educated their students and sent them doctors.

China's main aim then was to gain influence. Now China wants commodities more than influence. Its economy has grown by an average of 9% a year over the past ten years, and foreign trade has increased fivefold. It needs stuff of all sorts—minerals, farm products, timber and oil, oil, oil. China alone was responsible for 40% of the global increase in oil demand between 2000 and 2004.

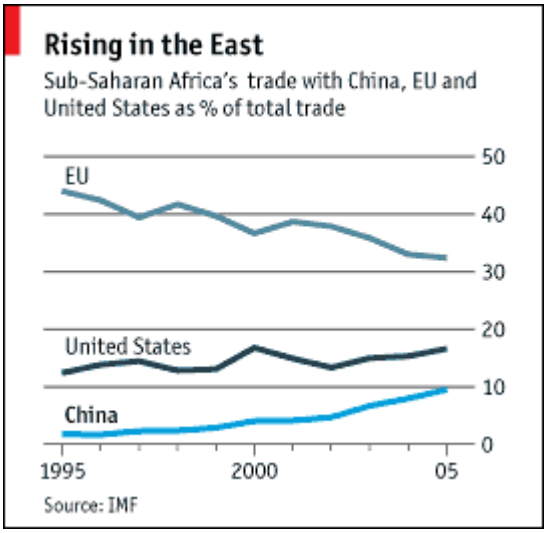
The resulting commodity prices have been good for most of Africa. Higher prices combined with higher production have helped local economies. Sub-Saharan Africa's real GDP increased by an average of 4.4% in 2001-04, compared with 2.6% in the previous three years. Africa's economy grew by 5.5% in 2005 and is expected to do even better this year and next.

Which countries are the main beneficiaries? For copper and cobalt, China looks to the Democratic Republic of Congo and Zambia; for iron ore and platinum, South Africa. Gabon, Cameroon and Congo-Brazzaville supply it with timber. Several countries in west and central Africa send cotton to its textile factories.

Oil, however, is the biggest business. Nigeria, Africa's biggest oil-producer, has been getting lots of attention. CNOOC, a state-owned Chinese company, paid $2.7 billion in January to obtain a minority interest in a Nigerian oilfield, and China recently secured exploration rights in another four. In Angola, which has now overtaken Saudi Arabia as China's biggest single provider of oil, another Chinese company is a partner in several blocks. China has shown similar interest in other producers such as Sudan, Equatorial Guinea, Gabon and Congo-Brazzaville, which already sells a third of its output to Chinese refiners.

Just the beginning

As a result, trade between China and Africa has soared from $3 billion in 1995 to over $32 billion last year. But China's commerce with the world also expanded over the same period, so Africa makes up only 2.3% of the total. This constitutes about 10% of Africa's total trade (see chart).



However, trade between China and Africa is expected to double by 2010. Although Europe remains Africa's main partner, its share has melted from 44% to 32% of the region's foreign trade within the past ten years, whereas America's share has, like China's, risen. For some countries, the redirection of exports has been dramatic. China now takes over 70% of Sudan's exports, compared with 10% or so in 1995. Burkina Faso sends a third of its exports, almost all of which are cotton, to China, compared with virtually nothing in the mid-1990s. China is now Angola's largest export market after the United States.

Africa has found more than a new buyer for its commodities. It has also found a new source of aid and investment. According to China's statistics, it invested $900m in Africa in 2004, out of the $15 billion the continent received. This was a huge increase (see chart), though most of it went to oil-producing countries. But its aid is spread more widely. It has cancelled several billion dollars of African debt, which has helped to build roads, railways, stadiums and houses in many countries.

This largesse is sometimes an entry ticket. In Nigeria China's promises to invest about $4 billion in refineries, power plants and agriculture were a condition for getting oil rights. In Angola a $4 billion line of low-interest credit enables Chinese companies to help rebuild the bridges, roads and so on that were destroyed in decades of war. The debt is repaid in oil.

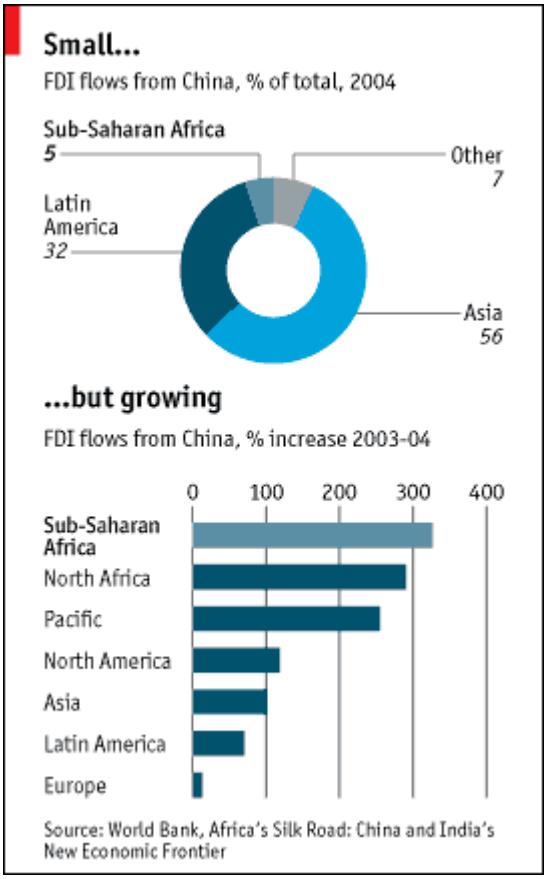
Fewer complications

For Angola, which has been keen to get going with the reconstruction of its infrastructure, China's straightforward approach is an attractive alternative to the pernicketiness of the IMF and the Paris Club of creditors, which have been quibbling over terms for years. So it is with many African countries, fed up with the intrusiveness of Europeans and Americans fussing about corruption or torture and clamouring for accountability. Moreover, the World Bank and many Western donors were until recently shunning bricks-and-mortar aid in favour of health and education. China's credit to Angola is not only welcome in itself. It has reduced the pressure from the West.

Thanks to China, therefore, workers from the Middle Kingdom

in straw hats are now helping Angolans to lay down new rails on the old line from Luanda to the eastern province of Malange. Another railway, from Benguela to Zambia, once used to carry copper, is also being rebuilt. China is happy: the work helps offset some of its trade deficit with Angola. The Angolan government is also happy: it is rebuilding its shattered economy at last.

For José Cerqueira, an Angolan economist, China is welcome because it eschews what he sees as the IMF's ideological and condescending attitude. “For them,” he says, “we should have ears, but no mouth.” Others are pleased because China is ready to pass on some of its technology. It is, for example, helping Nigeria to launch a second satellite into space. Some African officials, disillusioned with the Western development model, say that China gives them hope that poor countries can find their own path to development.



And now the snags

The love affair with China, however, may be sour as well as sweet. For countries that do not sit on oil or mineral deposits, higher commodity prices make life harder. Even for producers there are risks. A recent report by the World Bank argues that Africa's new trade with China and India opens the way for it to become a processor of commodities and a competitive supplier of cheap goods and services to Chinese and Indian consumers. But another report, from the OECD, a club of industrialised countries, argues that China's appetite for commodities may stifle producers' efforts to diversify their economies. Oil rigs and mines create few jobs, it points out, and tend to suck in resources from other industries. And if Africa is to escape its vulnerability to the capricious movements of world commodity prices, it must start to export more manufactures. On this the World Bank adds its own warning: China and India must end their escalating tariffs on Africa's main exports.

China is also bringing irresistible—some say unfair—competition to Africa. All over Africa Chinese traders can now be seen selling cheap products from the homeland, not just electronics but plastic goods and clothes. In Kamwala market in Lusaka a host of Chinese shops have appeared over the past couple of years. “Two years ago,” says Muhammad, a local trader of Indian origin, “I did not have time to sit down; now I'm sitting doing nothing.” Though his shelves are full of clocks and radios made in China, he blames his enforced idleness on the competition brought by Chinese traders.

Zambian and other African consumers do not share his despondency. They like Chinese prices. But in some countries consumers are less well organised than textile workers, and in South Africa the trade unions have succeeded in getting the government to negotiate quotas on Chinese clothing imports. Still, the power of China's productivity and economies of scale—never mind government subsidies—certainly hurts local industries. Textile factories in places like South Africa, Mauritius and Nigeria have been badly hit. In tiny Lesotho, where making clothes for Europe or America is the only industry around, this has been catastrophic.

The working conditions, as well as the prices, set by Chinese employers are also a concern to some Africans. The alleged ill-treatment of workers in a Chinese-owned mine in Zambia in July led to a violent protest in which several workers were shot. And many Chinese firms bring in much of their own labour, rather than hiring locals. China brought in thousands of its own workers to build the 1,860km (1,160-mile) Tazara railway between Lusaka and the Tanzanian port of Dar es Salaam in the 1970s. It was finished ahead of schedule, but Tanzania and Zambia still have to rely on Chinese technical help to maintain it. African hopes of technology transfer may be over-optimistic.

Human rights are optional

Some say China's involvement will erode efforts to promote openness and reduce corruption, especially in oil and mining. Nigeria insists that Chinese companies must respect its new anti-graft measures, and the latest bidding round for oil blocks in Angola has been the most open so far. In both countries it is

unclear whether China's presence is making corruption better or worse. It is clear, though, that China is not interested in pressing African governments to hold elections or be more democratic in other ways. That helps to explain why China directs so much money towards Sudan, whose odious regime can count on China's support when resisting any UN military intervention in Darfur. China invested almost $150m in Sudan in 2004, three times as much as in any other single country. When American and Canadian oil companies packed their bags there, China quickly stepped in, drilling wells and building pipelines and roads. The Chinese are supposed to be building an armaments factory as well.

China's lack of interest in human rights is something that President Robert Mugabe of Zimbabwe can also be thankful for. Shunned by the West, and with his country's economy in a shambles, he has turned to China for political and economic support—and got it. After he launched Operation Murambatsvina last year, in which 700,000 people had their homes or businesses destroyed, China neutered all attempts at discussion, let alone condemnation, in the UN Security Council. However, despite this, China may not want to squander any more money in a country that has no oil and few mineral rights left to dispose of.

AP

The Emperor's new clothes?

But China's friendship and support at the UN comes with one important political string attached: the endorsement of the one-China policy. To date 48 African countries have paid due obeisance to Beijing: Chad, Senegal and Liberia are the latest to have abandoned their recognition of Taiwan. The suggestion by Michael Sata, the main opposition candidate in Zambia's presidential election on September 28th, that he would have recognised Taiwan if he had won was enough to bring the first public intervention by China in the internal affairs of an African country; the ambassador said that China would consider cutting diplomatic relations if Mr Sata won (which he did not).

That is a warning to Africans that this new interloper in their continent is no more altruistic than its predecessors. Still, that does not mean China's involvement is bad and it is certainly not to be stopped. It is up to Africans to ensure that they get a fair deal from it. If so, both China and its African partners can be winners.

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Ethiopia

Soviet school

Oct 26th 2006 | NAIROBI
From The Economist print edition

More disturbing news from a former aid darling of the West

THE story is reminiscent of a cold-war spy tale: two diplomats risking everything to smuggle a dissident out of the country with the secret police just one step behind. Except that in today's Ethiopia the secret police proved to be one step ahead and Yalemzewd Bekele, a young human-rights lawyer working for the European Commission office in Addis Ababa, never made it. She was dragged aside by a plainclothes officer at the border with Kenya on October 19th and is now in prison and at risk of torture. The two colleagues from the commission who had taken her to the border were arrested and deported.

Ms Bekele's plight is probably connected to the arrest, on October 5th, of Alemayehu Fantu, a businessman. Mr Fantu was charged with distributing calendars with pictures of imprisoned opposition leaders on them. The calendars called for a campaign of non-violent civil disobedience to bring down the government—and seem to have driven the secret police berserk. A student was shot dead for handling them and those suspected of printing and distributing the calendars have been rounded up. Amnesty International, a human-rights pressure-group, is concerned that three of them may already have been tortured to death. Mr Fantu had difficulty walking when he appeared in court on October 12th. Senior diplomats believe he was injured by electric shocks.

The brutality is nothing new. Tens of thousands of Ethiopians were killed in the late 1970s by a Soviet-backed Marxist regime trying to cement its hold over an intensely religious, impoverished and ill-educated populace. But it is a disappointment. Ethiopia's prime minister, Meles Zenawi, had been close to Britain's prime minister, Tony Blair, and a favourite of aid donors. His government has shown some leadership in reducing poverty, not least by extending the reach of primary schools, health clinics, electricity and roads.

But the government's grip on power is slipping. An instinct for self-preservation may explain the former rebel fighters' return to Soviet methods. Things began to fall apart last year when a disorganised opposition disputed the results of a general election. Street protests followed in the capital in June and again in November. Around 80 people were believed to have been killed, including some police, after which opposition leaders, journalists, human-rights activists and businessmen were arrested. Many have since been charged with treason and genocide.

The government promised a speedy trial but has reneged, dragging out the process while keeping it far from view. Most of those arrested are still languishing in Kaliti prison in Addis Ababa. The cells there are baking hot by day, freezing by night, infested with roaches and mice, and thick with mud in the rainy season. The government has so far used a mix of spin and harassment of journalists (local more than foreign) to avoid international condemnation. But that may be changing.

An independent commission into the June and November killings has become an embarrassment. The government had stacked the commission with its supporters but eight out of ten of them still decided that the government had used excessive force. The commission members claim Mr Zenawi tried to get them to reverse their decision earlier this year; when that failed the government sought to bury the findings. The head of the commission and his deputy fled to Europe, fearing for their safety. Their investigation says at least 193 people were killed, nearly all by the security forces, including 40 teenagers, some shot at close range, others strangled. Some 20,000 young Ethiopians were said to be imprisoned in labour camps, though a government spokesman calls this “absolute rubbish”.

The government is spending more on its secret police as well as on state media. Well-placed sources claim an Israeli-trained unit now monitors e-mail and blocks opposition websites. Yet there is also disloyalty in the security apparatus. Berhanu Nega, the imprisoned mayor-elect of Addis Ababa, managed

to write a book in Kaliti entitled “Dawn of Freedom” that is now being widely distributed in *samizdat*. Some people say 200,000 of the opposition calendars have been sold, often for several times their cover price.

The government could claw back some credibility by releasing the political prisoners, but this is unlikely. And that credibility took another knock last week when Mr Zenawi was forced to admit, after months of denial, that Ethiopian troops had indeed been sent to intervene in the growing civil war in neighbouring Somalia. Donor countries are disgusted by the treason trial, but equally terrified that the country could once again fall miserably apart if they dare to stop their aid.

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Congo

The lesser of two evils

Oct 26th 2006 | KINSHASA
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Excitement and apprehension ahead of the presidential election

ONE running joke in Kinshasa is that it's like having to choose between cholera and the plague. But whether it is the incumbent president, Joseph Kabila, or Jean-Pierre Bemba, a former rebel, it is a choice Congo's voters are being asked to make on October 29th.

AFP

Totally in tune with Kabila

That millions of Congolese have this choice at all is a feat in itself. The run-off election is the culmination of years of negotiations and a tortuous three-year transitional period to end the 1998-2003 war, the bloodiest single conflict since the second world war.

Having just missed out on a first-round victory in July and now boasting the support of the third- and the fourth-placed candidates, Mr Kabila is the strong favourite. Rather than campaign himself, the quiet 35-year-old president has sent his wife and members of parliament out to do the work for him. They have been urging supporters in the president's native east who voted massively for him in the first round to do so again; there is little doubt that Mr Kabila will do well among his fellow Swahili-speakers. He has also recruited other politicians, including the son of Congo's late dictator, Mobutu Sese Seko, into trying to boost his vote in the Lingala-speaking west, where he still struggles.

With both candidates short of cash and taking extra precautions over security, Mr Bemba has also kept a low profile, sending a handful of lieutenants out to try to win over undecided voters. What little campaigning has taken place has been marred by local clashes between the two camps.

In August the announcement of the run-off was greeted by three days of fighting between the candidates' private armies. And there are fears of more to come. Many expatriates have left. The European Union, which has a force in Congo to support the UN's largest peacekeeping mission, sent more soldiers to the capital this week.

Diplomats are hurriedly trying to persuade both men to agree to grant a measure of personal, financial and legal protection to whoever loses. But so far, worryingly, these attempts have failed. Mr Bemba's camp says it is ready to sign on. Mr Kabila's men say that the president is in no position to grant immunity should Mr Bemba lose.

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Israel

A lion joins the lambs

Oct 26th 2006 | JERUSALEM
From The Economist print edition

Uncomfortable days for Israel's left

WHAT does it mean to be a left-winger in Israel these days? As the prospects of peace talks with the Palestinians have receded, many leftists have asked themselves that question, this week with even more urgency. Ehud Olmert, the prime minister, clinched a deal to bring Avigdor Lieberman's right-wing Yisrael Beiteinu into the governing coalition, to shore it up against possible collapse. Legislators from the centre-left Labour Party, the second fiddle in the coalition to Mr Olmert's Kadima, have been openly divided about whether to sit at the table with Mr Lieberman, whose views they find obnoxious, or leave and let him end up even more powerful as part of a rightist coalition.

What horrifies them about Mr Lieberman is not just his politics—he advocates stripping some Arab-Israelis of their citizenship and giving their towns and villages to the Palestinian Authority—but the fact that a man whose security experience consists of having been a corporal in the army, and who has proposed destroying all the Palestinian Authority's infrastructure and bombing Egypt's Aswan Dam, will now be formulating Israel's policy on a nuclear Iran. His new title is “minister for strategic threats”; pundits are joking that the chief strategic threat will be Mr Lieberman himself.

It will not be the first time Labour ministers have shared the cabinet table with Mr Lieberman, whose party originally spoke for ex-Soviet immigrants but now draws a third of its support from other poor and disenchanted right-wingers. However, Labour, which joined the Kadima-led government in the spring thinking it could set itself apart as more doveish and socially responsible, has failed on both counts. Its leader, Amir Peretz, has undergone the transformation—in public perception, at any rate—from gutsy trade-union leader to a defence minister in the thrall of the army and Mr Olmert. The objectors to Mr Lieberman fear that letting him in will further weaken any claim the party has to represent the centre-left, notwithstanding that Mr Peretz sweetened the pill by getting Mr Olmert to promise more state benefits for Arab-Israelis.

Farther left, Meretz, a peacenik party in the opposition, is equally divided over the leadership of Yossi Beilin, seen increasingly as ineffectual and wedded to old and unpopular peace agendas. Most of Meretz's leaders at first supported this summer's war against Hizbullah in Lebanon. When it turned into a debacle, they too were tainted. Zehava Galon, a parliamentarian who was the only one to oppose it publicly from the start, and who wants an international force to help separate Israel from the Palestinians, hopes soon to run for the party leadership, or even “the leadership of the left”.

That could be part of a wider change. Ephraim Sneh, an old-time Labour stalwart who supports Mr Lieberman's inclusion in the coalition (“It's worth trying for three months; what matters is what you do, not whom you sit with”), is talking of “a new framework for the centre-left”, based on a strong Israel, an early peace with the Palestinians and a “northern-European” economy. He hopes to draw wide support. Whether all this leads to new parties with fresh ideas or just a reshuffling is too early to tell.

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Russian politics

Wishing on a tsar

Oct 26th 2006 | MOSCOW
From The Economist print edition

The contest to succeed Vladimir Putin dominates Russian politics

Reuters

IN THE matter of deciding who will be its next president, as in others, Russia is not a real democracy. Vladimir Putin will nominate his successor like some non-hereditary monarch, and an election will merely validate his choice. But ordinary Russians do play a role: the Kremlin is currently offering them candidates in what is, in effect, a Russian-style informal primary. The “election” is not until early 2008, but the outcome will be known sooner.

The contest is already shaping events in Russia, where all political news is now studied through the refractive lens of the presidential succession. Conspiracy theories, many of which seem outlandish to outsiders, connect everything to the 2008 question: from the murder earlier this month of Anna Politkovskaya, a journalist, to the stand-off with Georgia and occasional purges of the bureaucracy.

When Mr Putin was levered into power by Boris Yeltsin's Kremlin in 1999-2000, he was portrayed as the antithesis of his predecessor: as sober, athletic, and grimly determined to prosecute the bloody war in Chechnya and wipe out terrorists “in the outhouse”. Six years on, his likely successors, whom Russia's state-controlled media are heavily promoting, represent contrasting ideas about the country's future.

Dmitry Medvedev, whom Mr Putin last year made a deputy prime minister, suggests a version of Russia as a modern, if troubled state. Mr Medvedev oversees Mr Putin's so-called national projects, pork-barrel initiatives in health, education, housing and agriculture. In public he talks mostly about domestic problems (albeit not usually the most pressing ones of rampant corruption, lawlessness and violent xenophobia).

The other main contender, Sergei Ivanov, the defence minister (and also a deputy prime minister) embodies a different notion of Russia's future: as a great but embattled imperial power. The recent spy spat with Georgia has boosted Mr Ivanov's profile, though perpetual scandals about corruption and brutality in the armed forces continue to tarnish it. The Kremlin, it seems, wants to influence the whole political spectrum. It is currently creating a new political party, to appeal to left-leaning and nationalist voters, but which will be as loyal as the slavishly dependable parliamentary majority.

Russia may not be a real democracy, but nor, as Dmitri Simes of the Nixon Centre in Washington, DC, says, is it an absolute tyranny. The Kremlin wants to anticipate the public mood, and is testing its candidates and the ideas they embody on television and in opinion polls. At the same time, it is

scrambling to ensure that no independent alternative emerges. Visiting Moscow last week, Condoleezza Rice, America's secretary of state, expressed concern about two of the Kremlin's methods: muzzling the media, and the haphazard application of a new law that regulates non-governmental organisations. The voting (and counting) will doubtless be closely orchestrated too. Russian liberals are helplessly depressed about their chances of disrupting the coronation.

Yet, for the Kremlin, there are still risks, and one of them is Mr Putin himself. The president's approval rating hovers just below 80%. This “ultra-popularity”, says Sergei Markov, a political consultant with Kremlin connections, looks like an asset for 2008: polls suggest that many Russians will vote for whomever Mr Putin tells them to. But some say that if they cannot vote for Mr Putin, they will vote for no one. His imperial style of government—ever the good tsar beset by under-performing ministers—has suppressed the popularity of others. Any successor may lack the clout to cope with a shock, such as a fall in the oil price, on which Russia's economy depends, or renewed mega-terrorism. Mikhail Kasyanov, a former prime minister turned would-be opposition leader, predicts a national crisis following a manipulated election.

Another risk stems from Russia's only real political competition: that among Kremlin factions. What looked like a peaceful transfer of power from Mr Yeltsin to Mr Putin turned out to have victims, in the shape of the Yeltsin-era oligarchs subsequently imprisoned or exiled. So the succession struggle is also a fight for influence, interests and freedom. Lilia Shevtsova, of the Carnegie Moscow Centre, speculates that an unbridgeable split within the elite might yet allow a flamboyant authoritarian challenger to emerge.

Or, more likely, it might encourage Mr Putin to stay in power. That does not necessarily mean changing Russia's constitution to remain in office for a third term, as a burble of supplications from regional politicians is urging. There are other ways, such as a redistribution of powers between the presidency, government and parliament. On October 25th, in a tsar-like televised phone-in, Mr Putin bolstered that idea by saying enigmatically that “with you [the voters] we can influence the life of the country” after 2008.

The Putin presidency shares with its predecessor one characteristic: opacity. Mr Putin mostly dodges awkward subjects. He may also be holding another candidate in reserve, to protect his successor from the current infighting. But Mr Putin is also more orderly than his predecessor. He will probably want to anoint his choice, perhaps by installing him as prime minister, by next autumn. An intensified public-relations campaign may start sooner. Russians may quickly discover what choice has been made on their behalf.

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The Holocaust in Ukraine

A glimpse of the abyss

Oct 26th 2006 | KIEV
From The Economist print edition

A glitzy night in Kiev to remember a tragic past

THE great, good and less good of Kiev gathered last week to honour an illustrious guest and an unlikely artistic collaboration. The guest was Steven Spielberg, and the occasion was the premiere of “Spell Your Name”, a documentary about the Holocaust in Ukraine. “I feel like I'm home,” said the director, whose grandparents emigrated from Ukraine. A group of elderly survivors and rescuers featured in the film blinked into the flashlights.

The A-list turnout included Viktor Yushchenko, Ukraine's president, his predecessor, Leonid Kuchma, and Viktor Yanukovich, whom Mr Yushchenko defeated during the “orange revolution” of 2004 but is now awkwardly reincarnated as Ukraine's prime minister. One attraction was Viktor Pinchuk, a canny tycoon (and Mr Kuchma's son-in-law), whose Jewish grandparents got out of Kiev in time. As well as financing the film, he is credited as joint executive producer, but says he always deferred to Mr Spielberg. Cynics saw “Spell Your Name” as part of Mr Pinchuk's effort to launder his reputation and win new friends in the post-Kuchma era. Perhaps; but Mr Yushchenko and the rest also attended because Ukraine's wartime history is still sensitive.

A few days before the premiere, in the streets of Kiev, communists scuffled with members and supporters of wartime partisan groups, who fought both the Germans and the Red Army and still crave government recognition as veterans. But like the Cossack leaders also revered by Ukrainian nationalists, the reputation of some partisan groups is tainted by the killing of Jews. Official Soviet anti-Semitism is gone, but the unofficial kind lives on. Leonid Serebriakov, an octogenarian who appears in the film, says he still hears of nasty anti-Semitic incidents.

For many ordinary Ukrainians, the Jewish tragedy is just one part of a century of pain, not least Stalin's 1930s famine that killed millions. There is also touchiness about Ukrainian collaboration with the Nazis. The film, which relies heavily on interviews recorded by Mr Spielberg's Shoah Foundation Institute, deals with that theme sparingly, balancing it with stories of Ukrainian heroism. It prefers impressionistic snatches of narratives to full-on horror, linking them with what Mr Spielberg calls a “visual poetry” of Ukraine: melting ice, empty railway carriages.

One legacy of the Soviet era is ignorance. In the film, a student wonders whether Jews are recognisable by their earlobes. There is little trace of the Jewish civilisation that once thrived in the villages of western Ukraine—nothing, in some places, except the marks left behind by unscrewed mezuzahs, the little prayer-scrolls that Jews attach to their doors.

Victims commemorated at the sites of mass graves are often recorded only as “Soviet citizens”. At the Babi Yar ravine in Kiev, where tens of thousands of Jews and others were killed, several competing memorials have been erected. “Spell Your Name” circles around the Yar, with glimpses and allusions—something too big to be confronted directly.

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Whaling

Rocking the boat

Oct 26th 2006
From The Economist print edition

Iceland unleashes its harpoonists

ALONG with pandas and tigers, whales are among the most charismatic of megafauna. They sing, they socialise and they look after one another. They are impressively big and surprisingly graceful. They seem somehow wise and sad. So when Iceland renounced a 20-year-old worldwide moratorium on commercial whaling, a predictable hullaballoo broke out.

AP

Good for dog food, bad for tourism

The Icelandic authorities are handing out permits to catch 30 minke whales, the most abundant sort, and nine rarer fin whales. That is on top of the 40-odd minkes already caught each year, supposedly for scientific purposes, although the meat eventually finds its way from the laboratory to restaurants and supermarkets. Iceland is not the only transgressor: Norway openly breaches the moratorium, while Japanese scientists claim the need to kill quite a few whales.

Environmentalists argue that both species are scarce, and the fin whale officially endangered. But Iceland says there are plenty more mammals in the sea. The International Whaling Commission (IWC), the council of whaling nations that imposed the moratorium, reckons there are 174,000 minke whales in the North Atlantic, and 30,000 fin whales.

Polls suggest that Icelanders cherish the right to bear harpoons, in part, presumably, because they think the IWC is trying to deprive them of it forever. The commission is divided between the Captain Ahabs of Japan, Iceland and Norway, and whale-huggers like Sweden and New Zealand. The IWC will probably never allow whaling to resume unless Japan succeeds in its effort to stack the membership with sympathetic but implausible countries, such as landlocked Mongolia. The ban is particularly irksome to Iceland, whose fisheries are thriving, thanks to careful management; those of some of the most zealously anti-whaling countries such as Britain have collapsed, due to over-fishing.

That said, whale-watching brings Iceland over $15m a year, and is growing. Tour operators worry about a repeat of a recent incident in Norway, in which a whale was harpooned in front of horrified eco-tourists. Polls also reveal that few Icelanders enjoy eating whale, which tastes like stewing steak infused with tuna oil. Whaling nations have amassed a blubber mountain, despite desperate measures, such as mixing the stuff into dog food. It is the principle, apparently, that counts.

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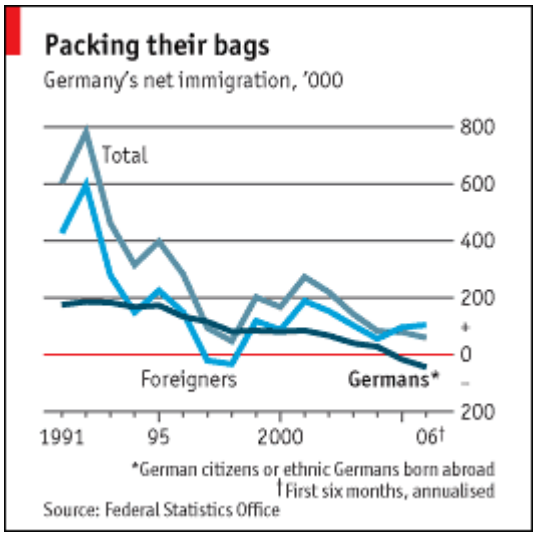
Germany: land of emigration

Auf wiedersehen, Fatherland

Oct 26th 2006 | BREMERHAVEN
From The Economist print edition

For decades, foreigners found work in Germany. Now Germans are going abroad in search of jobs



FROM the windswept quays of Bremerhaven, a German port city on the North Sea, more than 7m sailed away in search of a better life, among them Germans, Russians and Scandinavians. For those wanting to relive the great 19th-century journeys to America, the destination for many of those emigrants, the city now offers an "experience museum" to give visitors a real taste of leaving home.

At the German Emigration Centre they can walk though replicas of the wharves where loved ones said their final farewells, ships' cabins and the arrival room at New York's Ellis Island. For many Germans back then, departure was a permanent breach with the homeland, as emigrants had to give up their German citizenship.

Until recently, all this would have been a journey into a bygone age. Germany, after all, has long been a powerful magnet for immigrants, attracting millions of foreign "guest-workers", many from Turkey. The fall of the Berlin Wall in 1989 set in motion a further movement of people: Germans moving from the degraded east to the affluent west, ethnic Germans "returning" to the homeland, Jews leaving the oppression of Soviet times and other East Europeans seeking work in the most accessible part of the West.

Now the trend is reversing. The tally of foreigners and ethnic Germans moving to Germany has declined sharply, while the number of Germans leaving the country is accelerating. In 2004 more than 150,000 Germans reported to their town halls that they were going abroad—the highest number since 1884. The real figure is almost certainly much higher. Germany, once the economic engine of Europe, is on the point of becoming a country of net emigration. The museum in Bremerhaven may soon need a new wing with an aeroplane cabin or high-speed railway carriage, today's mode of departure.

This turn of events is not without irony. Until recently, politicians bickered about too many immigrants. Now it is emigrants they worry about. "A terrible development," said Roland Koch, the premier of the state of Hesse, who once won an election by opposing a proposal to allow dual citizenship for Turks living in Germany. Business leaders are even more anxious. "More and more young people are turning their backs on Germany," fretted Ludwig Georg Braun, president of the German Chamber of Industry and Commerce.

On the surface this may look like a case of overdone German angst. In the first six months of this year 69,000 Germans left the country, but 47,000 came back. The net outflow was 22,000 people, almost insignificant in a country of 82m people. However, according to Simone Eick, director of the Bremerhaven museum, emigration is likely to become a long-term trend.

The modest figures mask a more serious problem: brain-drain. Hard numbers are difficult to find, but anecdotal evidence suggests that many more academics are leaving Germany than are arriving, in contrast with countries such as the United States and Sweden that have a net "brain-gain". According to a German medical organisation, about 12,000 German doctors now work abroad, many of them in Britain and Switzerland, which last year replaced the United States as the workplace of choice. Austria now ranks as the third-favourite destination.

In part, this is due to globalisation. German university students usually spend at least one term abroad and often speak a second language fluently. For the highly skilled, it does not matter much whether they work in Berlin, Munich, London or New York. Their stories of success encourage others to follow suit, explains Ms Eick.

There is also something deeper at work. With unemployment stuck above 10% and growth lagging behind the rest of the European Union, many young Germans feel that their country offers them too few opportunities. In June an article on emigration in *Manager Magazin*, a business monthly, provoked a flood of comments from Germans all over the world, turning its website into a forum on emigration. A typical posting complains about “ossification, a culture of jealousy and the arrogance of the powerful”.

The mood may improve if Germany's economic recovery continues. There is no question, though, that the country must learn to attract and retain the highly skilled (and highly mobile), whether German or foreign. Yet this week the federal government turned down proposals to make it easier for talented foreigners to work in Germany. Only 138 people defined as “highly qualified”—such as engineers and entrepreneurs—settled in Germany in the first quarter of this year, out of a total inflow of 123,000 foreigners. For their part, local authorities and universities seek to attract bright foreigners, for instance by creating “welcome centres” to help them get residence permits, find homes and enrol in language classes.

One more development explains why it is a good idea for Germany to try to stem the flow of emigrants: its neighbours are getting nervous. In Switzerland, doctors are already complaining that Germans are taking the best jobs. Austria has introduced a quota for foreign students, because Germans are starting to crowd out natives at medical schools (where they often perform better than Austrians in entrance exams). If they are not careful, Germans may become the unloved “guest-workers” of tomorrow.

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Reforming the Bundeswehr

New model army?

Oct 26th 2006 | BERLIN
From The Economist print edition

Military review misses the point

WHEN Germany's cabinet endorsed a new strategy on military and security this week, it chose its spot carefully: the Bendlerblock. The defence ministry is not only the former headquarters of the Nazi-era Wehrmacht, but also the place where the conspirators who tried to kill Adolf Hitler in 1944 were executed.

Modern Germany's message is twofold: it intends to play a bigger military role around the world, but it will not revert to militarism. Formally abandoning the primary task of defending the country's borders, the Bundeswehr plans to create a 14,000-strong force able to act simultaneously in five separate international missions.

However, the cabinet did not spell out the circumstances in which Germany is prepared to intervene. The Bundeswehr may have greater means. But will politicians have the political will to act, and the ability to make Germans accept that their soldiers can die in war and do nasty things?

In recent years Germany has often sent its troops abroad, but its servicemen have rarely been at the centre of the action. In Afghanistan they stay in the relatively calm north instead of helping their NATO colleagues fight the Taliban in the south; in Lebanon, Germans patrol at sea but not on land. The problem is not just one of history. In 1994 the Constitutional Court ruled that parliamentary approval was required to send troops abroad.

So far, 64 soldiers have died on foreign missions since the early 1990s, but none was killed in real combat. To their horror, Germans are seeing a darker side of their soldiers. A former Guantánamo Bay prisoner, a Turkish citizen who grew up in Germany, has accused members of the country's special forces of being involved in his torture in Afghanistan in 2002. And this week a tabloid published pictures of German soldiers desecrating human remains near Kabul—creating a bigger sensation than the news of the army's reform.

Germany still struggles to accept that military missions are not just a form of development aid, although attitudes may be changing. After years of dithering, the government will at last erect a national memorial to the 2,600 German soldiers who have died since 1956. Where? Near the Bendlerblock, of course.

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Albanian economy

Good times, at last

Oct 26th 2006 | TIRANA
From The Economist print edition

An unexpected boom in Albania will benefit the Balkans

Get article background

IT IS not hard to find bad news in Albania: the country is corrupt, the state is weak and organised crime is strong. Yet over the past five years the country has undergone a little-noticed but remarkable transformation. The chaos and violence of 1997, precipitated by the collapse of pyramid schemes that wiped out many people's savings, seems unthinkable today.

Brightly coloured blocks of flats and offices have sprouted all over Tirana, the capital. Roads across the country are being rapidly repaired and extended. Even Vlore, once a wretched, pot-holed, crumbling coastal town crammed with Kurds, other foreigners and Albanians—all waiting to be smuggled to Italy—is enjoying a share of the renaissance.

A campaign against people trafficking, including a ban on speedboats, has largely choked off that trade. Some of its proceeds have gone into construction and legitimate businesses. With a reduction in lawlessness, hotels and restaurants now cater to ethnic Albanian holidaymakers from neighbouring Kosovo and Macedonia.

The relative stability of the past few years has helped Albania attract foreign banks. These have introduced such novelties as mortgages, which in turn have helped fuel the construction boom.

When politicians from the European Union talk of halting enlargement, or announce restrictions on workers from prospective new members, Albanians don't worry much. Although there are few reliable statistics, about a third of its population of just over 3m is thought to be living abroad, mainly in the EU: at least 600,000 in Greece, more than 200,000 in Italy and probably another 200,000 elsewhere. Expatriates are believed to be sending home some €1 billion ($1.25 billion) a year, and their cash has financed construction as well as consumer spending. So have the proceeds from organised crime, though police sources say education campaigns have sharply reduced the number of girls sold into prostitution abroad, having been duped into believing they would work as cleaners or nannies.

Unemployment officially hovers around an uncomfortable-sounding 15%; but joblessness is twice as high in Macedonia, and even higher in Kosovo.

Today the big worries are the future of the economy—remittances may not create many sustainable jobs—and the behaviour of Sali Berisha, the prime minister. Critics complain that, since his return to power last year, he has been attempting to control public life, for instance by trying to sack the prosecutor-general. “Berisha does not care about either the law or democracy,” argues Mustafa Nano, an influential Albanian columnist. But some of Albania's institutions seem more capable of withstanding the pressure these days.

Tensions in the Balkans will rise in coming months as Kosovo, inhabited mostly by ethnic Albanians, moves towards independence. But in Albania itself there is little interest in the notion of a Greater Albanian state. Given that the collapse of 1997 had a direct effect in igniting war in Kosovo, greater wealth and stability in Albania is important for everybody in the Balkans.

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Charlemagne

Europe, Russia and in-between

Oct 26th 2006
From The Economist print edition

Russia's “near abroad” is becoming Europe's neighbourhood

NORTH of the Caspian Sea, Europe seems a world away. The steppe stretches into Asia. A statue of Genghis Khan stands in the region's main town, Uralsk. The Lesser Horde (an administrative division of the Mongol empire) was proclaimed here.

Yet near this statue stands a house where Russia's great poet, Alexander Pushkin, stayed. And through the vast landscape runs the Zhaiyk river, which meanders down from the Urals, Europe's traditional eastern boundary. As you cross westward, the sign on the bridge says simply “Europe”; as you return, “Asia”.

Nursultan Nazarbayev, the president of Kazakhstan, says that, if his country ever applied to join the European Union, it would have a better claim than Turkey. That is because more of its territory lies west of the river Zhaiyk than there is Turkish land west of the Bosporus.

The margins of Europe lend themselves to games about where the continent ends, but they are more than a curiosity. Dealing with Russia and reducing European dependence on its oil and gas has become one of the main preoccupations of the EU. Relations with the Kremlin have become trickier of late. Last week's Russia-EU summit in Finland turned ugly, with Vladimir Putin saying Russia was no more corrupt than Spain, and pointing out that “mafia” is an Italian word, not a Russian one.

It is sometimes thought that Europeans can do little to rein in a petrodollar-fuelled Russia, beyond issuing the occasional mild rebuke. But the EU is not without clout. It may not be able to influence the Russian government's behaviour inside the country, but it can try to limit the consequences outside. It can do this by changing the way it treats the countries sandwiched between itself and Russia—the former Soviet republics that Russia calls its “near abroad” and which the EU calls its “neighbourhood”.

The EU has never really had a policy towards its neighbours, except enlargement. So when new members from central Europe joined the club in 2004, Europeans faced an unfamiliar problem: for the first time, they were jostling up against countries that they could not necessarily influence with the inducements of membership, either because they were too big or too un-European. Moreover, these new neighbours were not a relatively coherent group like the ex-communist states of central Europe; they formed an arc of instability from Belarus in the north-east, round the Caucasus and along North Africa to Morocco.

To deal with this motley bunch, the EU invented a “neighbourhood policy”. The overall aim was to

encourage stability and liberal reform. But this was an umbrella term covering two entirely different groups: countries to the south which would never join the EU and where the main European concerns were immigration and Islamic radicalism; and those to the east, where people thought of themselves as European, wanted policy advice as much as money and believed that they stood a chance of getting into the EU one day. This policy was incoherent, of course. But that did not matter—until recently.

New political forces are at work. One is the emergence of a more assertive, even aggressive, Russia. Now the EU needs to stabilise its eastern neighbours not only for their own sake, but to fend off Russia and diversify away from its energy. The other factor is enlargement fatigue within the union and the public reaction against the prospect of even more countries joining the 25-member club (soon to be 27). This means that countries such as Ukraine no longer believe vague EU hints about eventual membership; they want something more substantial.

Germany is trying to get the EU to offer just that. It wants to change and expand Europe's engagement with the neighbours, by extending bits of the single market eastwards: to Ukraine, to bind it closer to the EU; and even farther east to Kazakhstan, which has one of the ten largest oilfields in the world. The EU's foreign-affairs commissioner, Benita Ferrero-Waldner, is drafting a co-operation agreement with Kazakhstan, in effect claiming Central Asia's largest and most successful country as part of Europe's neighbourhood.

One should not expect too much from all this. It is true that Kazakhstan is potentially an alternative energy provider—but in ten years' time it will probably still be only a potential source. The country is landlocked. Almost all exports go through Russia. A pipeline across the Caspian (skirting Russia) has been mooted but is years from being built. Asked about the EU's role in Central Asia, a former foreign minister from Kyrgyzstan said dismissively: “The EU? We don't know anything about the EU here.”

The Ukrainians consider themselves part of Europe, not its fringe. They see even glorified neighbourhood status as a glass half-empty. Yet Russia could react neurotically to EU meddling in what it sees as its backyard. As it has shown repeatedly, the Kremlin is perfectly prepared to use energy prices, and the threat to cut off supplies, as a means of putting political pressure on other countries. It is now trying to slow down Ukraine's membership of the World Trade Organisation.

Hug them close

Does that mean greater EU engagement with its neighbours amounts to a policy of high risk and low reward? Countries on Russia's rim have as much reason to welcome European influence as the Europeans have to seek a role. For almost all of them, the EU is their largest trading partner and they want to reduce dependence on Russia (much more onerous for them than dependence on Russian gas is for the EU). And all, with the possible exception of Georgia, see closer ties with the EU as a way of diversifying risks rather than antagonising Russia.

This is one of those occasions when the EU can be more influential than its constituent parts. Germany, France or Britain can do comparatively little to contain Russian meddling. An EU of 25 and still growing can remind Russia that its “near abroad” is also Europe's neighbourhood.

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Poor whites

The forgotten underclass

Oct 26th 2006 | DAGENHAM AND LEICESTER
From The Economist print edition

Muslims and blacks get more attention. But poor whites are in a worse state

Get article background

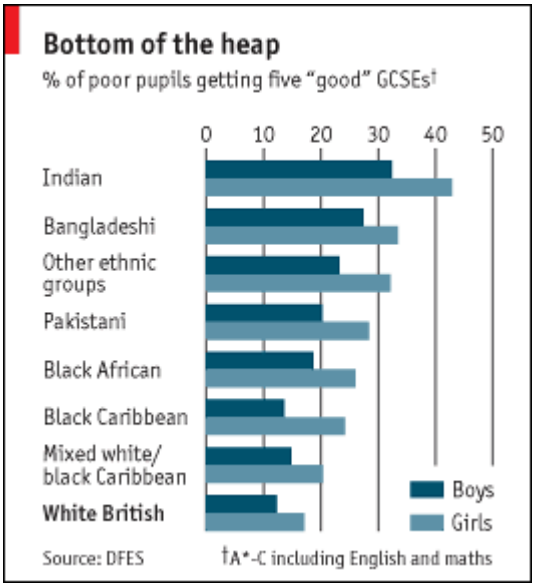
TONY PERRY remembers the first time he saw a black child. So exotic did the baby seem in mid-1950s Dagenham that locals flocked to see what they described, without malice, as a “piccaninny”. These days, strangers of all hues are moving to the working-class neighbourhood in east London. The white natives, who blame everything from stabbings to the difficulty of obtaining public housing on immigrants, are not pleased. Many of Mr Perry's friends talk about leaving. What is worse, the new arrivals are more qualified and have better prospects than the people among whom they have settled.

Apart from election campaigns, when rising support for far-right political parties in areas such as Dagenham causes alarm, the traditional working class is largely overlooked. When politicians say that some communities are failing to integrate with mainstream society, they mean Muslims from the Indian subcontinent. When campaigners complain that schools are failing some children, they often cite black boys. Yet the nation's most troubled group, in both absolute and relative terms, is poor, white and British-born.

The troubles begin at school. Last year white teenagers entitled to free school meals—the poorest tenth—did worse in crucial GCSE examinations than equally poor members of any other ethnic or racial group (see chart). In the borough of Barking and Dagenham, the contrast is sharper still. Just 32% of all white children there got five “good” GCSEs last year, compared with 39% of blacks and 52% of Asians. In Leicester, just 24% of whites got five decent GCSEs.

By tracking tens of thousands of poor children, academics at Bristol University have pinpointed the problem. When poor whites are tested at the age of seven, they fare only slightly worse than poor blacks, and better than poor Pakistani and Bangladeshi children, many of whom are struggling with English. By 14, whites have overhauled blacks and continue to lead the

other two groups. But at 16, when futures are decided in the national exams, the white children do worst of all. Poor Indian and Chinese pupils, who have been ahead all along, increase their lead dramatically.



No more jobs for the boys

Clearly something happens to white children between the ages of 14 and 16 that does not happen to others. That something is that they write off the value of education in doing well in life. At the same point in their lives, or even earlier, their parents and grandparents came to the same conclusion. John Simkin, who went to school in Dagenham in the 1950s, says the ready availability of factory work made for uninterested and rowdy classrooms. “We didn't believe there was any connection between our school work and what we would do as adults,” he says.

White youngsters who think they can leave school with few or no qualifications and walk into a job are not wholly deluded. Richard Berthoud, who studies the subject at Essex University, points out that whites at all levels of education (including the unskilled) are slightly less likely to be unemployed than are others. But poorly qualified whites face two problems. First, education trumps ethnicity. It takes only a dash of additional qualifications to enhance the job prospects and pay of a black or Asian person. And the competition is hungrier for qualifications: whites are less likely to stay at school beyond the age of 16 than any other group.

The second problem is that unskilled whites tend to go into the wrong line of work. Many toil in factories: in 2001 white British men comprised 89% of the overall workforce but 93% of the manufacturing workforce. Unfortunately for them, the sector has been in long-term decline. Manufacturing now employs just 18% of all male workers, down from 30% two decades ago. Ford, which employed 30,000 workers at its Dagenham car factory in the early 1970s, now requires 4,000—and new recruits for its engine plant are expected to have three good GCSEs, in maths, English and a science.

Immigrants and their offspring, by contrast, have found jobs in services and expanding public-sector activities. They are over-represented in health and social work, finance and the hotel and restaurant trade. With the exception of Pakistanis, they tend to be where the work is. The 2001 census showed that 42% of Indians, 55% of Bangladeshis and 79% of black Africans live in London. And they usually have a positive attitude to education. Many immigrants with humble jobs come from middle-class backgrounds and are determined that they, or their children, will return to that class. Others come from rural backgrounds; but they, too, push their offspring upward. Tahir Abbas of Birmingham University believes such immigrants are all the keener to rise in society because this opportunity was denied them in Bangladeshi and Pakistani villages.

During the past few decades the white working class has experienced a social upheaval of its own, which has contributed to the problems of those now doing so badly. In 1980 the roughly three-in-ten families who lived in social rented housing were given the right to buy their homes at subsidised rates. By 2004 some 1.7m had done so in England. Sales were swiftest in the smaller, nicer housing estates and in the parts of Britain where the private property market was strong. In east London the buyers were those whom Mr Perry calls “the elite of Dagenham”—people who, he says, “thought they were better than everyone else.” In other words, the aspirational working class.

Some of those who bought their own homes stayed in east London. Their properties are distinguished by stone cladding, leaded lights and, in some cases, Greek columns. But a great many others have sold up and moved to the fringes of Essex. There they indulge in even more exuberant feats of exterior decoration, send their children to good schools and, in many cases, vote for the Conservative Party. They have become middle class.

The departure of such strivers has removed the leaven from the housing estates that they quit. Doris Connolly, who has lived in Leicester's New Parks estate for more than 50 years, says that her street initially seemed heavenly. Its two-storey houses were solid and wide, with generous front rooms and indoor bathrooms. But her once friendly neighbours have been replaced by others who are loud and troublesome. It is as though the estate has become a social dumping-ground.

The estate is currently most famous for an incident that occurred in September, when two guard dogs attacked and killed a baby in its cradle. The media flocked there and reported that it was violent and unpoliceable. That was an exaggeration. There is plenty of crime in New Parks, but mugging and serious violence are comparatively rare. Between April and September this year burglaries outnumbered robberies eight to one (the average for England and Wales is three to one). The reason, believes Andy Sharp, a local copper, is that so many people know each other by sight.

One reason poor British whites have escaped scrutiny is that they are less associated with serious criminality than other ethnic groups, particularly Afro-Caribbeans. British blacks are disproportionately young and tend to live in big cities, which are heavily policed. They may be more likely to commit the sort of extravagantly violent crimes that attract stiff sentences. It is this reason, rather than any racial bias in the criminal-justice system, that explains why they are over-represented in prison compared with whites.

But whites actually commit more crime. A large survey carried out by the Home Office in 2003 found that white men were more likely to admit to having broken the law in the past year than were blacks, Asians or people of mixed race. Fully 18% of whites aged 10 to 25 admitted to a violent crime, and 15% said they had committed a theft. Young whites are also most likely to take Class-A drugs (the most serious kind).

Despite their occasionally sharp language, most poor whites are not deeply racist. More children are now born to one white and one Afro-Caribbean parent than to two Afro-Caribbean parents. Even in west Leicester, a solitary middle-aged Jamaican man can walk into a pub on an almost entirely white housing estate without fear of trouble.

Working-class whites do not, however, warm to those who seem to encroach on their privileges. The political fuss over east European workers (see article) notwithstanding, they worry less about competition for jobs than about public services. In Beaumont Leys, a bleak housing estate north of New Parks, locals have been known to break into houses where refugees are settled and to steal their council-provided furniture—or, as they see it, restore it to its rightful owners. Other responses to the new arrivals have been more violent. It is a surreal spectacle: people who live in some of the worst housing in Britain fighting to keep others out.

Received wisdom suggests that immigrants blend into the host society, gradually infiltrating the economy until they become socially indistinguishable from natives. Those who live in white working-class areas see things quite differently. As John Blackmore, a councillor who represents New Parks, puts it: “Asians seem to be the new middle class”.

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BAE Systems

Changing places

Oct 26th 2006
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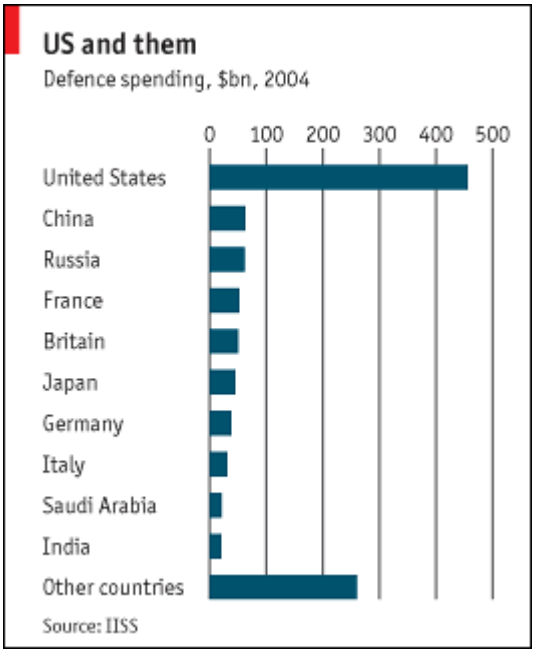
Britain's national defence champion may soon be American



THE divorce has been so long in the making that few eyebrows were raised when Lord Drayson, the defence-procurement minister, said he was “relaxed” at the prospect of BAE Systems, Britain's biggest defence contractor, leaving the country. More important than who owns BAE, Lord Drayson told the *Financial Times* in an interview published on October 23rd, is where the company's skills and intellectual property reside.

Lord Drayson's comments are of more than passing interest to BAE, whose heritage can be traced back to the firms that built the Spitfire and Hurricane fighters that duelled with German aircraft in the Battle of Britain. The firm has long wanted to move to America where defence spending is almost ten times higher than in its home market (see chart). But it can do so only if the British government lifts a veto barring takeovers and foreign management of BAE established when the company was privatised in 1985.

Although BAE already sells more weapons in America than it does at home, it is shackled by a security agreement that requires its business there to be run by citizens of that country. Not even Mike Turner, the company's chief executive, is allowed to know the details of its most sensitive American contracts. This constraint is becoming untenable now that almost two-fifths of its sales are there.

And although the company is well rooted in America—its directors include Anthony Zinni, a former general, and Richard Kerr, a former deputy director of the Central Intelligence Agency—it still bumps up against protectionist sentiment. “The only way BAE can move its business forward is by becoming American,” says Paul Beaver, a defence analyst.

The company coyly says that it does not plan to become American until half of all sales are made there and Americans hold half its stock (it reckons they now hold about a third of the company), but it may not have long to wait. Last year it completed the $4.2 billion acquisition of United Defense, a maker of infantry carriers, to become the seventh-largest defence contractor in America. The purchase was cannily timed. More than $17 billion has recently been set aside by the defence department to repair and replace the tanks and vehicles that are being worn out by constant use in Iraq.

At the same time BAE is scaling back some of its businesses in Europe, where defence spending has fallen. This month it sold its 20% stake in Airbus, a troubled maker of (mostly) civilian jets, freeing up cash for more American acquisitions.

But the move presents its own risks. Although BAE tries to present itself as a local company in each of its markets, ownership still matters in the defence industry. In tying itself to America BAE may be forced to withdraw from other markets. For two decades it has been sustained by the flow of £43 billion ($80 billion) from the Al Yamamah contract to supply Saudi Arabia with jets. The order would probably have gone to American firms but for that country's powerful pro-Israeli lobby.

Moving abroad may also threaten its detente with the Ministry of Defence. After years of clashing with BAE over cost overruns the government has now begun treating it like a national champion of old, says

Keith Hartley, who heads the Centre for Defence Economics at York University. The government may not be quite as generous when signing contracts if it becomes just another American contractor.

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Migration from eastern Europe

Shutting the door

Oct 26th 2006
From The Economist print edition

There will be no welcome mat for Bulgarian and Romanian workers

EPA

Turned away

WHEN the European Union expanded to the east in May 2004, Britain was the only large country to open its labour market to workers from the eight new member states. Together with Ireland and Sweden, it gave up the right to impose restrictions lasting up to seven years.

On October 24th, that open-door policy was slammed shut for Bulgaria and Romania, which are due to join the EU in January 2007. John Reid, the home secretary, announced a battery of controls, which have been designed to keep out all but a trickle of migrant workers from the union's two new members.

The policy reversal had been foreshadowed in August, when ministers started to drop the heaviest of hints that Bulgaria and Romania would be treated differently. It followed an embarrassingly wrong prediction the government had published about the likely migration from Poland and the other seven countries that joined in 2004. This suggested that the net inflow of workers would be only 13,000 a year until the end of the decade. However, figures published in August showed that 427,000 migrants from eastern Europe had registered for work between May 2004 and June 2006. Allowing for the self-employed took the true figure closer to 600,000 according to Tony McNulty, a Home Office minister.

The government's new controls are designed mainly to prevent low-skilled Romanians and Bulgarians from working in Britain. Only 19,750 will be allowed to work in just two industries, agriculture and food processing (and citizens from non-EU countries will no longer be allowed to work in those sectors). A handful of highly-skilled workers will be welcome; and skilled migrants can be employed provided that they get work permits. Students will be allowed to work part-time.

The open-door policy may have ended but it is an open question how effective the new labour-market controls will turn out to be. Bulgarians and Romanians will still be allowed to visit Britain. The government cannot prevent them from working if they are self-employed. The figures for migration from the first eight countries in eastern Europe show that this could prove a significant chink in the door.

Those working illegally can be fined £1,000 ($1,876); and their employers £5,000. Mr Reid has also doubled the funding to enforce compliance. Whether these sanctions will bite is open to doubt given the difficulty of policing jobs. The Transport and General Workers' Union fears that “rogue employers” will favour Bulgarians and Romanians because they will offer “scared, compliant labour” without any legal

protection. Some may just declare themselves self-employed.

The Bulgarian and Romanian governments are offended by the controls. Research from the Institute for Public Policy Research, a think-tank, suggests that most Bulgarians and Romanians would in any case rather work in Mediterranean countries where many of their compatriots are already employed.

The wave of migration from eastern Europe has been good for the economy. However, the government has been rattled by growing opposition to the newcomers. One concern is that they are out-competing native unskilled workers. Another is that they are putting excessive strain on the public services. Politics has trumped economics.

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Electricity grid

Big spender

Oct 26th 2006
From The Economist print edition

The rise of renewables will change the power network

HIGH oil and gas prices, together with worries about both energy security and climate change, are reshaping the power industry. There are high hopes that new technologies for generating electricity will be able to reduce dependence on fossil fuels. Less attention is paid to the transmission network that links consumers with power plants, notably the pylons that march up and down the land, scarring or enhancing views depending upon one's taste. But Britain is about to make the biggest upgrade of its electricity grid in more than half a century.

The network, which was privatised in 1995, now has three owners: National Grid, Scottish and Southern Energy, and Scottish Power. These are currently negotiating with Ofgem, which regulates the industry, about how much they can charge the power generators for access to the electricity grid between 2007 and 2012. National Grid says that it plans to spend an extra £3 billion over this period—a sum of money that would buy eight new 1,000MW power plants.

Around half of the investment will be spent renovating the existing grid. Britain has one of the most robust networks in the world, according to Robert Hull, Ofgem's director of transmission. But much of the equipment is reaching the end of its design life and needs replacing. “We're not noticing any impact on reliability just yet,” says Nick Winser of National Grid. “But we want to stay ahead of the game.”

The remaining investment is more controversial. The government wants renewable sources of energy like wind power to make up a fifth of total power generation by 2020. Most of this will come from wind turbines, which are often best sited far from the existing network. Building power lines out to remote and windswept bits of northern England and Scotland will be expensive. The total bill for preparing the grid for renewable energy is expected to be around £1.5 billion.

Not everyone is happy with these plans. National Grid requires a prospective new generator to pay a sizeable deposit for the new connection (which also involves work on the grid itself to take the extra load). Raising the money can be difficult, especially for modestly sized wind farms. “Often the payments can be as much as the project itself is worth,” says Gordon Edge of the British Wind Energy Association.

The underlying problem is that renewables are an inherently more expensive source of energy. As Richard Green of Birmingham University points out, a wind turbine typically produces 30% of its theoretical maximum output in a given year, compared with 60% for a fossil-fuel plant. This means in effect that renewables need to pay the grid roughly twice as much for each unit of electricity that they deliver.

Various solutions are being touted. One option is to link several wind farms together in one connection hub, allowing several developers to split the deposit. The wind-energy lobby would prefer to see the arrangements changed altogether. It may well win ministerial support. If Britain is to switch a big chunk of its energy supply to renewables, a price will have to be paid for using a naturally less reliable, if more politically secure, source of energy.

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Energy efficiency

Out of the window

Oct 26th 2006
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Wasteful houses are a bigger problem than spendthrift habits

WHILE National Grid prepares for a future with more power stations, the government is keen to reduce the need for them. On October 26th David Miliband, the environment secretary, gave a speech that discussed, among other things, how to improve energy efficiency in the household sector.

There is much to be done. Households consume over a quarter of Britain's electricity and produce a similar share of its carbon-dioxide emissions. On October 23rd the Energy Saving Trust, a government-funded outfit paid to worry about such things, reported that out of five big European economies, the British were the worst offenders for leaving on lights, computers and other gadgets when they were not in use.

However, such sins pale in comparison with Britain's leaky homes. Heating takes up 60% of the total power used by households, and much of this energy goes to waste as well. According to Brenda Boardman of Oxford University's Environmental Change Institute, Britain is generally accepted to have the worst insulated houses in western Europe: “The rule of thumb is that we're about 30 years behind the times.” Partly, she says, that reflects the 21st century's love of 19th-century homes, which were constructed when people did not expect the whole house to be cosy and bracing draughts were seen as a health feature. New rules require new houses to be much more energy-efficient. However, a low rate of homebuilding means that it will take many decades for these improvements to percolate through the housing stock.

If homes are to be made less leaky soon, existing ones will have to be tackled. That should be easy since homeowners have good financial reason to reduce their energy use. The trust reckons that a typical family could save £300 a year; the work would pay for itself within five years.

Yet despite official exhortations, energy efficiency has proved a tough sell. Ignorance is one difficulty. Wonky incentives are another: tenants, for example, are unlikely to pay to improve a landlord's property. Ms Boardman also puts some of the blame on inflated claims made by over-zealous manufacturers, which may have put the public off sensible measures like wall insulation and more efficient lightbulbs.

Consumer reluctance has encouraged more radical ideas. One, floated in Mr Miliband's speech, is to persuade power firms to change their business model, selling comfort instead of kilowatts. “People aren't fussed about how much power they buy,” explains Philip Sellwood, chief executive of the trust. “If energy suppliers sold a service—a lit and heated house, rather than units of gas or electricity—then they would face incentives to provide it as efficiently as possible.” In theory, such companies would even pay to improve their customers' homes, cutting their own costs in the process. One is already operating in Woking, a green-minded town; another is planned to start in London.

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Exporting education

English lessons

Oct 26th 2006
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Old schools are finding new markets abroad

INDEPENDENT schools have long wooed Chinese parents. Pupils from China make up two-fifths of foreign children educated privately in Britain. But now schools are moving to the students.

Dulwich College and Harrow have already led the way in establishing offshoots in China. These international schools have, however, mainly taught expatriates (of all nationalities). They have also been able to teach children from Hong Kong but, crucially, not those from mainland China.

The lure of China

Now the first Anglo-Chinese school teaching Chinese children from the mainland (but not expatriates) is about to be set up. The Girls' Day School Trust (GDST), a network of 28 independent schools, has announced plans to expand eastward. In a joint venture with a Chinese partner, GDST will open a school in Shanghai in 2008, twinned with and bearing the name of Oxford High School, one of its members. Dulwich College hopes to follow suit soon with a similar venture, as will Nord Anglia, an educational business that already has two large schools in Shanghai.

The business opportunity arises from the attractions of an English education to Chinese families. Fluency in English and internationally recognised qualifications are keenly sought as China opens up to the world. Tradition adds to the brand appeal; at Harrow's offshoot in Beijing, the youngsters chant the school song. The two schools that Dulwich College has opened feature its iconic bell-tower as a unifying theme, says Graham Able, its headteacher—and extensive playing fields.

Most of the private schools operating abroad license their brand names to a local partner. The GDST deal will be different, as the charitable trust will jointly own the school with its Chinese partner.

Although schools with overseas operations are tight-lipped about the exact size of their international profits, one says that they run into six figures and another that they offer “healthy returns”. Dulwich College uses such income to finance bursaries for poorer pupils in its London school.

The international market is not confined to China. Nord Anglia has four schools in central Europe and is opening one in South Korea. Albert Hudspeth, general secretary of Cobisec, which represents many British international schools, says that market growth is unremitting thanks to the thirst for an English education. In the past year, for example, 20 schools opened in Dubai and Kuwait.

But not everyone agrees that foreign expansion is the way forward. The Chinese government retains tight control over the curriculum, which creates tricky problems for British educators. Nord Anglia had to spend months designing a joint English and Chinese curriculum for its new school in Ningbo City. Eton has resisted the temptation to expand abroad. Tony Little, its headteacher, worries about the possible “reputational risk” if standards cannot be maintained overseas. He wants to focus on the school rather than dissipating energy on risky foreign ventures.

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Self-harming

Silent scourge

Oct 26th 2006
From The Economist print edition

Why more and more teenagers are hurting themselves

WEDGE was ten years old when he started branding his skin with hot pieces of metal. At secondary school, he used a pair of compasses and a razor blade to hurt himself. When he confessed to university friends about this self-affliction, he was surprised to find that several of them also harmed themselves.

Surveys show that teenagers deliberately injure themselves to a worrying extent. In a study of 6,000 schoolchildren aged 15 and 16, researchers at the universities of Bath and Oxford found that 7% had harmed themselves in the previous year. More than half cut their skin; others hit and burned their bodies. Girls are much more likely to injure themselves deliberately than boys: 11% of girls admitted to self-harming in the preceding year, compared with 3% of boys.

The practice has been growing fast, according to Chris Holley, a nurse at St George's Hospital in Stafford and a specialist in self-harming. “When I was young,” she says, “I hadn't even heard of it; now all teenagers know all about it.”

Keith Hawton, director of the Centre for Suicide Research at Oxford University, who led the study of the 6,000 teenagers, says that in most cases self-harming is a way to mitigate unhappiness. Researchers at King's College London and Manchester University have shown that the number of depressed British adolescents has risen substantially in the past 25 years.

The increase has several causes, ranging from stress because of higher educational expectations to more drug abuse and binge-drinking. Peer-group pressure also plays a part. Mr Hawton finds that teenagers are more likely to hurt themselves if their friends do so. Self-harming may also have a paradoxically alluring image for susceptible teenagers.

If Britain has a problem, it is not alone. Similar studies to Mr Hawton's have been conducted in six other countries. Four of these found roughly the same rates of self-harming among teenagers (and a similar preponderance among girls). Only Hungary and the Netherlands showed markedly lower levels.

There are no national guidelines in the health service on how doctors and nurses should treat self-harmers. In hospitals, nurses have tended to confiscate knives and razors to prevent cutting. But there is a growing belief that this may be counter-productive. “If someone really feels they need to hurt themselves and this is denied, the situation may only get worse,” says Ms Holley. She is working with the Royal College of Nursing to draw up guidelines for working with self-harmers.

Outside hospitals, it is becoming easier for people like Wedge to get help. He tackled his depression with counselling and medication and now runs lifeSIGNS, a charity that helps youngsters drawn to self-injury. There is no simple prescription. Indeed, those who study self-harming increasingly believe that it should be treated as a symptom of other underlying problems rather than focusing on the practice itself.

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Bagehot

In defence of the young

Oct 26th 2006
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Paying too much attention to the demands of the elderly is dangerous for society

THIS week David Cameron gave a widely praised speech on society's responsibility to the elderly. He argued that for too long they had been “airbrushed out of the picture” and that a community with too many young people and not enough older ones was likely to be socially unstable. If the Tory leader was simply making a pitch for the support of electorally powerful pensioners, he could not be faulted. But as an analysis of what is actually happening in Britain it was badly skewed.

Many very old people have a tough time. Despite Labour's best efforts, there are still pockets of pensioner poverty, especially among women; and too many old people, as Mr Cameron observed, are dumped in residential-care homes that often leave a lot to be desired. But the next generation, the baby-boomers born after the war, many of whom are now approaching retirement, may be among the luckiest in history. Their children, on the other hand, face a far more uncertain and stressful future and risk being largely ignored by politicians.

Except, that is, by David Willetts, the Tories' education spokesman and for some years its resident expert on reforming the pension system. In his contribution to a timely pamphlet (“2056: What Future for Maggie's Children?”) from Policy Exchange, Mr Cameron's favourite think-tank, Mr Willetts gives warning that, whereas class conflict used to dominate politics and conflicts of culture and identity are today's worries, the looming danger is generational conflict.

There are several reasons for the baby-boomers' good fortune. Many of them were enrolled in occupational pension schemes that were linked to their final salaries. In 1995 some 5m private employees were building up entitlements in defined-benefit schemes open to new members. Now there are only around 2m. Lord Turner's Pensions Commission said last year that it expected such schemes more or less to disappear from the private sector over time.

The standard response of companies to the pension crisis of recent years has been to close their schemes to new members, plug the deficits from profits and set up less generous defined-contribution plans for new staff. As Mr Willetts says: “This adds up to a very dramatic shift in resources across the generations.”

Then there's housing. Baby-boomers getting their first foot on the housing ladder enjoyed both

mortgage-tax relief and the debt-gobbling effects of inflation. Then, when inflation fell in the 1990s, they benefited again from a step jump in the value of their biggest asset as low interest rates stimulated a prolonged housing boom. By contrast, their children are typically having to wait nearly ten years longer, until their mid-30s, to become first-time buyers and are then likely to be stuck with mortgage debt for most of their (longer) working lives. At the same time they will be making steeper pension contributions and paying off student debts that their parents were spared.

Nor can today's young count on sharing in their parents' wealth when they die. Inheritance tax, which used to be levied only on the wealthy, now hits many middle-class estates. According to the Halifax bank, if the tax's threshold is increased only by inflation, 4.6m homes will exceed its value by 2020. Recent research by the Joseph Rowntree Foundation, based on a survey of 2,000 adults, found that two in three “plan to enjoy life and not worry too much about leaving a legacy”. The hedonistic individualism that took root in the 1960s means that most baby-boomers are happy “skiers”—Spending the Kids' Inheritance”.

The same adverse inter-generational transfers are taking place through the public finances. The growth of borrowing under Gordon Brown and the costs of servicing private finance initiative (PFI) projects will fall most heavily on the next generation of taxpayers.

Nothing could demonstrate more starkly older people's grip on political power than the priority given to the health service by first Labour and now the Tories. The Conservative Party's website is covered with “Stop Brown's NHS Cuts” logos (after the government has nearly doubled health spending in real terms since 2000). Mr Cameron declared in a recent keynote speech: “Tony Blair once explained his priority in three words: education, education, education. I can do it in three letters: NHS.” The average annual cost to the health service of looking after someone aged over 85 is six times that of someone aged between 16 and 44. Overwhelmingly, the NHS is a service for the elderly.

Out-numbered, out-voted and ignored

None of this should be very surprising. As well as being lucky, the baby-boomers are numerous compared with their offspring. As Mr Willetts points out, they were born at a rate of 800,000 a year, while themselves managing to reproduce at an annual rate of only 650,000. Their political influence has been further magnified by the fact that they and their parents vote in large numbers, whereas their children by and large don't.

In the same Policy Exchange pamphlet, John Curtice, a psephologist, points out that it is not unusual for the young to be less interested in politics and less inclined to vote than their elders. However, many young people, having been turned off voting by declining ideological differences between the parties and a series of highly predictable election outcomes, may never take up the habit. Out-numbered and out-voted, they are likely to become ever more sceptical about getting things done through conventional politics.

Political parties, which are in the market for votes, cannot be entirely blamed for putting the claims of the elderly before those of the young. But it is short-sighted, unhealthy for democracy and wrong in itself. Having secured only a fifth of the votes of 18-44-year-olds in 2005, the Tories, of all parties, need to pay attention to the interests of younger voters.

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Communism

Comrades, come rally

Oct 26th 2006 | JOHANNESBURG, NEW DELHI AND ROME
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Corbis

Fifty years after the crushing of the Hungarian uprising, communism is thriving

HISTORY is perhaps on their side after all. At their annual conference next month, delegates from 70-odd Communist parties will be in a buoyant mood. Memories of Soviet crimes are fading, America's stock is falling and the injustices of global capitalism make an increasingly easy target. Communists always had good songs. Their political tunes of justice and solidarity may still sound hollow to some, but they now resonate more widely.

The comrades' label has become remarkably elastic. Some retain both a monopoly of power and a belief in socialism (eg, Cuba); some are dictatorial, but enthusiastic capitalists (China, Vietnam). Those that had a monopoly of power but lost it sometimes stay true to old beliefs (like the Czech party). Others have kept the name but dumped everything else (Moldova's Communists, uniquely for eastern Europe, regained power through the ballot box, promised to create another Cuba, and then turned pro-Europe and anti-Kremlin).

Another group spent much of their lives as the persecuted opposition to an undemocratic regime, and retain an aura of heroism as they operate out in the open (South Africa, Iraq). Lastly come those who have simply won a share of power in an established democracy (Italy, India).

Without a Soviet Union to act as ideological enforcer, the communist tribe is more scattered than ever, and differences matter much less. Boundaries that were once stark are now fuzzy. India's once-warring Communist parties are now electoral allies and coalition partners. Babis Angourakis, the international officer of Greece's party, the KKE, says that origins are no longer an issue: any party “still fighting for a socialist transformation of society and defending the proletarian revolution described by Marx, Engels and Lenin” is welcome at the annual gatherings that his party launched in 1998. Eurocommunists can rub shoulders with Stalinists who would once have called them traitors; even different brands of Maoists turn up, ranging from the Chinese party to former admirers of Albania's Enver Hoxha.

Friendship has its limits. Nepal's Maoists, who have taken power in large parts of the country after a lengthy rebellion, have little to do with their nominal mentors in China. They will not be present at this year's get-together; other parties view their armed struggle with distaste.

One difficulty is which model to defend. Almost all communists praise Cuba, the last outpost of what was once the Soviet empire. But North Korea's bizarre mixture of personality cult and paranoia is a harder sell: most defend it as a victim of American imperialism; only a small minority insist that it is a workers' paradise. The world's biggest communist country, China, looks like the sort of society Marx criticised, not the one that he wanted to create. Libero Della Piana, the national organiser of America's Communist Party, says dryly that the Chinese enthusiasm for profit “is a source of discussion in the world movement”.

But the biggest problem, history, is no longer such a vote-loser. Many who lived in their shadow may regard the hammer and sickle as akin to the swastika, but elsewhere communism prompts not revulsion but an attractive frisson of naughtiness. It is a good way of annoying conservatives, Atlanticists and plutocrats. European communists such as Mr Angourakis are cock-a-hoop about their success in blunting an attempt by the centre-right parties in the European Parliament last year to equate communism with Nazism.

No more tradition's chains shall bind us

In much of the former Soviet empire, relabelled former communists plus their intelligence officers and other henchmen hold power. The Hungarian prime minister, Ferenc Gyurcsany, infuriates his anti-communist opponents (who boycotted this week's official commemoration of the 1956 uprising) with his close family ties to the old Soviet-installed regime. Nobody else seems to care.

Reuters

Give me that old-time religion

Some of that hold on power is fuelled by communist slush funds adeptly recycled into capitalist business. Hundreds of millions of dollars of such money have been flooding into Romania and Bulgaria as they prepare to join the European Union. “They're not stupid, these guys”, says one Balkan security official. “They got the money out to Austria before they lost power. And now they are sure that it will be a safe investment here, they are bringing it back again.”

The most spectacular example of the erosion of the anti-communist taboo is in Italy, historically the home of the most powerful communists in an advanced economy. No fewer than three parties with communist roots are part of Romano Prodi's left-of-centre government. Giorgio Napolitano, Italy's president, and Massimo D'Alema, the foreign minister, were both leading members of the old Italian Communist Party.

Its Eurocommunist members mostly re-emerged as the Democrats of the Left, the biggest party in Mr Prodi's coalition. But two groups of hardliners are also in the government. Communist Refoundation, the bigger of the two, got its best result for years in the parliamentary election in April, 7.2% in the election to the Senate, giving it 27 seats out of 315. Its leader, Fausto Bertinotti, is a strikingly patrician figure (a habitual feature of Italian proletarianism). He successfully appealed to a generally leftist constituency of pacifists, anti-globalisers and gay and lesbian campaigners. The party's most flamboyant lawmaker is a transvestite actor and singer. All very different from the puritan spirit of traditional communism.

The Refounded Communists have muscles to flex. Mr Bertinotti took from the Democrats of the Left the speakership of the lower house, a post that brings prestige and influence over the parliamentary timetable. Italy's tax-and-spend budget shows his influence, as does the halt to privatisation, which

would have hurt his core constituency of public-sector employees.

In South Africa, by contrast, leading members of the Communist Party have turned into stern fiscal conservatives in the African National Congress-led government. But the rank and file, often active in the trade-union movement, is blocking labour-market reform, and chafing at an orthodox economic policy that it sees as too harsh on the poor and unemployed. The party is threatening to stand on its own in future elections, an option that would look more realistic if the ANC were to split.

India's two Communist parties are more powerful and more contradictory. Both use communist symbolism, but in practice support the mixed economy and rule of law. Their nationwide appeal means that they are an important electoral force at national level; their block of 50-odd seats forms a key part of the governing coalition led by the Congress party. They also run three states: Kerala, Tripura and West Bengal. This latter state has been ruled by the Communist Party of India (Marxist) for 29 years, with a remarkable mixture of strong party discipline and ruthless electoral tactics. Traditional left-wing policies such as land reform have now been supplemented under the state's chief minister, Buddhadeb Bhattacharjee, by a keen search for foreign investment, and support for privatisation—ideas that the party shuns at a national level.

Solid pragmatism in south Asia does little to excite the comrades in the wider world. Mr Angourakis reserves his greatest enthusiasm for the onward march of radical leftism in South America. In Nicaragua, Daniel Ortega, once a hardline leader of the Soviet-backed Sandinista regime, is the favourite in the presidential election on November 5th. Venezuela's Hugo Chávez calls himself a “21st century socialist” but is adored by communists round the world, and returns the favour with subsidies for Cuba and comrades elsewhere in Latin America, especially Nicaragua.

Mr Angourakis says prospects are at their brightest since the “collapse” of 1991. The fate of hundreds of millions of people has worsened since the “counter-revolution” of that year, he says. Now the failure of “imperialist wars” in Afghanistan and Iraq creates new opportunities.

Hang on—the Iraqi and Afghan Communist parties were among the most determined foes of Saddam Hussein and the Taliban respectively; America's invasion has put the Iraqi Communists in government. But on another point, most communists are clear; they eschew any alliance with jihadism or Islamic fundamentalism. Such opportunism, says one true believer disdainfully, is only for Trotskyists.

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Cold war survivors

Let each stand in his place

Oct 26th 2006 | PRAGUE
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Some cold war skeletons are in surprisingly good health

MOST cold war institutions shrivelled in the 1990s, along with their superpower backing. The big communist front outfits that fought propaganda wars, awash with cash and stuffed with spies, have fizzled away in a mixture of apathy and swindles. This week's court-enforced auction of a hulking concrete pile in the heart of Prague belonging to one of them, the International Union of Students, was halted amid squabbles among its dozens of creditors.

On the other side of the barricades, the World Anti-Communist League changed its name and retreated to Taiwan, where it now, oddly, pursues cross-straits ties with “Mainland China”. The Captive Nations' Committee, which united émigré stalwarts, has all but folded, though the White House still dedicates a week in July to countries enslaved by communism. America slashed the budget for Radio Free Europe and Radio Liberty (RFE/RL). Library shelves emptied of anti-communist tomes: *Questions of Peace and Socialism* ceased publication; so did *Problems of Communism*.

But RFE/RL continues trenchant coverage of Russia, and has launched new services in Arabic and Persian. Meanwhile solidnet.org, a website that co-ordinates the orthodox communist parties' international ties, may not be the Comintern, but it offers a pungent foretaste of a get-together in Lisbon next week: “Dangers and Potentialities of the International Situation, the Imperialist Strategy and the Energy Issue, the People's Struggle and the Experience of Latin America, the Prospect of Socialism.”

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Liberation technology

Mobiles, protests and pundits

Oct 26th 2006 | BUJUMBURA AND LONDON
From The Economist print edition

Mobile phones are changing politics faster than academics can follow

UNTIL recently, killers in Burundi found it easy to cover their traces; they just tossed the bodies into a river where crocodiles would eat them up. But in August residents of Muyinga province acted fast when they saw fresh corpses drifting downstream; they used their mobile phones to contact NGOs, who in turn tipped off the United Nations, whose soldiers got to the scene fast enough to recover some forensic evidence.

AFP

My name is legion, for we are many

The use of mobiles as a tool of “empowerment”, even in the poorest and worst-governed parts of the world, is not always so grisly. The cruder kinds of electoral fraud, relying on poor communications between the capital and the boondocks, are now much harder. Even with minimal resources, monitors can count the voters and conduct exit polls—and then phone their findings to a radio station before the authorities stuff the ballot boxes. Such methods have helped make elections a bit cleaner in places like Ghana and Kenya. Meanwhile, in Europe's darkest corner, Belarus, text messages call youngsters to surreal acts of resistance, such as (to take a recent example) gathering to eat ice cream.

Howard Rheingold, an American technology guru, has devised the pun “smart mobs” to describe the way mobile telephony—and especially texts—make it possible for aggrieved groups to act and react in an ever more nimble way.

Chroniclers of cellular people power identify two big landmarks: the rallies that toppled President Joseph Estrada of the Philippines in 2001, and South Korea's presidential election a year later, when text messages among the young brought a surge of support for President Roh Moo-hyun. In both those countries protests are still convened by text message not just at critical times, when national leadership is at stake, but to highlight almost any sort of grievance.

For Europeans “mobile democracy” came of age with the Spanish election of March 2004, immediately after a terrorist attack in Madrid: the Socialists rode to power on a wave of text-driven anger with the ruling conservatives. In America some claim the same happened at the Republican convention in 2004, when text messages helped protesters play cat-and-mouse with the New York police.

It is also true that modern telephone technology has its uses, for sophisticated armies, as a weapon of war. The Chechen leader, Jokar Dudayev, was traced and killed by the Russians through his satellite phone; and the Israelis used an exploding handset to assassinate a leading Palestinian bomb-maker.

But in the competition to use mobiles in a more benign way, ordinary people often prevail over their masters. When governments try to crack down on the mobile phone as a popular tool of communication, their efforts usually go haywire. During the SARS epidemic in China, for example, the authorities tried to censor text messages that mentioned the disease, but their attempt proved easy to circumvent.

In the run-up to this year's elections in Congo, all the parties used mobiles to summon the faithful. That prompted the security services to shut down several numbers used by opposition leaders. But in such a mobile-savvy country, the effect of such clumsy repression was short-lived.

In short, the use of mobiles in protest and politics and even banking (see article) is evolving faster than governments' efforts to control it. Academics also find the phenomenon baffling, though they are studying it hard. Four eggheads with links to California's Annenberg School of Communication will publish next month a book based on a two-year study of mobile phones and society. Their punchy conclusion? “When the dominant institutions of society no longer have the monopoly of mass-communication networks, the dialectics between power and counter-power is, for better or worse, altered for ever.” True enough, though the average teenage texter might put it better: “whn u cn fon u r in chrge 4vr”.

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Press freedom

The hazards of reporting risk

Oct 26th 2006
From The Economist print edition

The rich aren't always free, nor the poor unfree

THREATS to press freedom range from religious zealots to secret policemen, via the shadowy forces that organised the recent killing of Anna Politkovskaya, a brave Russian reporter. And journalism is perilous not only in wild, chaotic countries. The latest annual survey by Reporters Sans Frontières (RSF), a media watchdog, claims that conditions have worsened in several rich Western countries while many poor ones are enjoying greater freedom.

Some will find the report implausibly harsh towards the United States, which has fallen nine spots to 53rd place on the annual RSF press-freedom index. Considered less free than countries such as Mozambique, Mali and Panama, America's rating has been downgraded thanks to growing tension between the administration and the media—caused, for example, by pressure on reporters to reveal sources. It was also dented by the jailing of Josh Wolf, a blogger who refused to hand over film of a political protest in California. Freedom House, which monitors democracy and other civil liberties, puts America at a more flattering 17th place in its latest press-freedom survey.

Not that RSF scores its home country much more highly. France has dropped five places, to 35, in response to searches of journalists' homes and newsrooms and attacks on many media workers during riots. Denmark's press freedoms frayed in the row over cartoons depicting Muhammad: the culture editor of the newspaper that published the cartoons was sent on leave and journalists needed police protection. In Japan (down from 37th to 51st place) *kishas*, or exclusive press clubs, froze out reporters from humbler outlets.

A long-term loser is Lebanon, whose RSF ranking has fallen from 56th to 107th place in the past five years. Other poorish countries are doing better—at least in RSF's view. Ghana jumped 32 places this year to rank 34th. Benin, Haiti and Panama climbed higher too. News organisations in such places may be poor, but reporters are determined and enterprising. Cheap computers and internet access have also helped.

Giving scores to journalists being captured in Iraq, ostracised in Japan and slain in Russia may miss the point. But RSF is probably right to reach its gloomy conclusion: press freedom is in retreat from a very odd coalition of foes.

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The art of the impossible

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From The Economist print edition

Bridgeman

A morose France has fallen behind its competitors. But there is nothing inevitable about its decline, argues Sophie Pedder: all it needs is political will

“SOMETHING seems very wrong with this country. Once the very model of a modern major power—stable, rich and smug—it appears beset now by political and economic instability and by civil unrest and disorder. One observer has even taken to calling it 'the sick man of Europe'. Hardly a month passes without the appearance of a new book or learned article on the decline and imminent demise of a once proud country.”

Alarmist talk about France has become commonplace. Home-grown titles such as “France in Freefall”, “Gallic Illusions” and “France's Malheur” crowd the bookshelves. Politicians hold seminars with titles such as “The Origins of the French Disease”. “Declinism” has become a school of thought. Pessimism prevails. Fully four-fifths of the French tell pollsters that they think “things are getting worse.”

But the opening quotation, seemingly so apt for morose France today, is not about that country at all. It was written in 1979 by Isaac Kramnick, an American political scientist, and refers to Britain.

The 1970s were Britain's decade of self-doubt, not so unlike the first decade of the 21st century is turning out to be for France. The country was paralysed by a sense of terminal decline. The mainstream left was beholden to its militants, union friends and class warriors. Politicians were preoccupied by the distribution of wealth, not its creation. Strikes were as crippling as taxes. Industrial jobs were going to lower-cost countries and academic brains to America. Britain was uncomfortable about its place in the world.

Now it is France's turn. The country is gripped by a belief in its own decline. It sees itself as a victim of globalisation, regarding markets as a threat and profits as suspicious. It has a short working week, militant unions and high unemployment. The opposition Socialist Party, in its official programme for next spring's presidential and parliamentary elections, pledges to renationalise the electricity utility, raise the minimum wage, enforce the 35-hour week more vigorously and reverse tax cuts.

Moreover, the creed of anti-liberalism and anti-globalisation is shared by both left and right. The centre-right government of Dominique de Villepin is irredeemably protectionist, fending off foreign predators at every turn. The president, Jacques Chirac, a Gaullist descendant, has called liberalism a greater menace for Europe than communism. France is troubled by its diminished voice in the world and fretful about immigration at home. Fear of change is pervasive.

Just as Britain battled through its winter of discontent in 1978-79, when rubbish went uncollected, school gates unopened and ambulances undriven, France has fought its way through a series of social upheavals in the past 18 months. First, its electorate revolted over the European Union in May 2005, rejecting a new constitution for the European project that its own countrymen co-founded. Next, its multi-ethnic underclass revolted against exclusion, with 20 consecutive nights of rioting in nearly 300 *banlieues* across the country, forcing the government to declare a state of emergency. Most recently, its students and unions revolted against insecurity, holding countrywide strikes, university sit-ins and protest marches to contest a plan to make it easier to hire and fire the under-26s.

Some historians trace this turbulence and fiery rejectionism back to the collective spirit of the 1789 revolution and the French fondness for the drama of confrontation (as in 1830, 1848 and 1968). Others suggest that these events are symptoms of a dysfunctional democratic system in which the street is a more efficient theatre of protest than parliament.

Popular malaise has certainly been simmering for a while. Since 1978 the French have not re-elected an incumbent government. They have gone through 12 prime ministers when over the same period Britain and Germany have each had a mere four heads of government. When the far-right Jean-Marie Le Pen was voted into the 2002 presidential run-off against President Chirac, it was an early distress signal. That vote was partly against immigration, a theme the National Front leader has long exploited. But it was also a protest against what the republican French, with a disarming nod to elitism, call the “political class”: the cosy governing caste in Paris. In that election, 35% of the votes went to the political extremes or protest parties on the left and right. The message to mainstream politicians was plain: we've had enough of your empty promises.

Three reasons for gloom

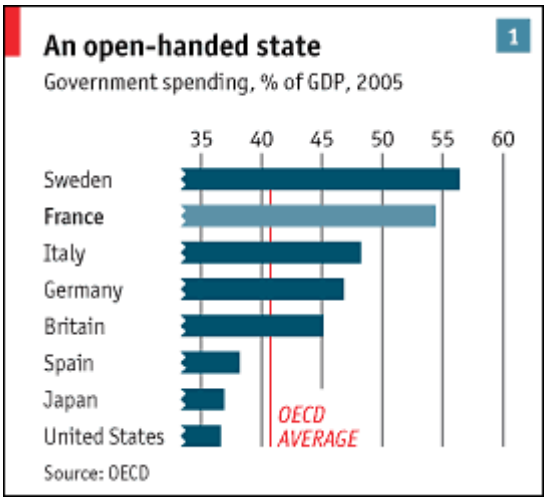
Why are the French so restless? The answer is threefold. First, their economy has lost ground. For example, France's GDP measured at current exchange rates has been overtaken by Britain's, which is now 5% bigger (even though the two countries' populations are much the same). Back in the late 1970s it was the other way round: the British economy was only three-quarters the size of the French one. Over the past 25 years, in terms of GDP per head at current exchange rates, the French have dropped from seventh place in the world to 17th. Even allowing for things France does well, such as health care and welfare, the 2005 United Nations Human Development Index ranked it 16th, down from eighth in 1990. The French feel the slippage keenly. Polls show that “loss of purchasing power” is one of their top concerns.

Second, France's heavily planned economy has reached its limits. In the past, the French dirigiste model,

which relies on a strong centralised state in the pre-revolutionary tradition established by Jean-Baptiste Colbert, Louis XIV's finance minister, served the country well. It speeded up reconstruction after the second world war. It delivered the *trente glorieuses*, or 30 years of post-war prosperity. And it laid the ground for the rapid transformation of the economy into an industrial powerhouse.

Even today, elements of dirigiste planning have helped to set France up for the modern age. Its high-speed TGV train network reaches into new corners each year: to Strasbourg in 2007, from Lyon to Turin by 2018, with projects to extend lines to Bordeaux, Rennes and Perpignan. As Thierry Breton, the finance minister, points out, France's early decision to invest in nuclear energy, which accounts for 78% of its electricity production, has turned a country short of fossil fuels into a net electricity exporter.

Yet the planned society relies crucially on an intelligent and efficient state, and over the years the French version has become untenable: too many bureaucrats, supported by too many taxes, impose too many rules in too many overlapping organisations. Despite all this effort, there is little sign that the public sector in France is any more efficient than in other rich countries. French public spending accounts for 54% of GDP, compared with an OECD average of 41% (see chart 1). One in four French workers is employed by the public sector. Public debt amounts to 66% of GDP, compared with 42% in Britain, and over the past ten years has grown faster in France than in any other EU-15 country. The baby-boom generation is leaving behind a poisoned legacy: as the title of a recent book puts it, “Our Children Will Hate Us”.



Too top down

Moreover, in such a hierarchical system people too often expect solutions to be provided from the top. For example, whereas Google was devised by two graduate students at Stanford University, a rival search engine with the unpronounceable name “Quaero” was ordered by the French government from, among others, two big French companies, Thomson and France Telecom. CNN was founded by Ted Turner, an American entrepreneur in Atlanta; a new French challenger to the cable television network, France 24, which is due to start broadcasting shortly, was invented by Mr Chirac and is financed with government money.

The problems have been building up for some time. Thirty years ago, Alain Peyrefitte predicted that the *mal français*—essentially, a bureaucratic mentality—would stifle creativity and innovation and entrench resistance to change. Another critic wrote in 1994 of a “France suffering from a more profound sickness” than anybody then imagined: a “heavy and inert” state machinery that, if unreformed, would “block the evolution of society”. The prescient author? Mr Chirac.

Even so, politicians have consistently failed to explain to the citizens why the country cannot afford to go on as before. This is the third source of French electoral dissatisfaction. Instead of making the case for change, successive politicians have preferred to blame, and thus to discredit, outside forces—usually Europe, America or globalisation. “The French political class has constructed a wall of lies against the globalised world,” comments Nicolas Baverez, author of “France in Freefall”. No wonder there is no consensus for reform.

Yet this survey will argue that French decline is not inevitable, any more than British decline was inevitable in the 1970s. There is nothing that necessarily predisposes the French to conservatism or resistance to change. Just because political leaders in the past have failed to push through bold reforms—Mr Chirac himself, in 1986-88; Alain Juppé, a former prime minister, in 1995—does not mean that the country is unreformable. The unruly French do not make the task easy, but winning them over is a question of political leadership—the courage to level with voters and tell them why things need to change.

The parallel with Britain is plainly inexact. For a start, France is rather better placed than Britain was in the 1970s. Public finances may be under strain, but there is no financial crisis of the sort that forced Britain to go cap in hand to the IMF in 1976. Corporate Britain at the time was ailing; corporate France now is thriving. The CAC 40 stockmarket index reached its highest level for five years this year and profits are at record levels. French firms are buying up companies across Europe. Both these factors

should help France to rebound more rapidly than Britain did. Moreover, France has the second-highest birth rate in the European Union, sparing it some of the demographic worries preoccupying countries such as Britain, Germany and Italy.

Change need not mean trampling on values that the French cherish. Some of those who defend the status quo argue that France is a civilised country that has simply chosen different priorities. Like a misunderstood teenager, it wants to do things its own way. It still believes in solidarity and social cohesion, in small farmers and local markets. It does not want to abandon its poor to the streets and its shopkeepers to Wal-Mart.

Yet economic efficiency and social justice need not be incompatible. The Netherlands, Ireland, Finland, Sweden, Denmark and Canada have all revived once-flagging economies without destroying their welfare system or way of life. France's long dole queues and troubled *banlieues* are proof that, by keeping things the way they are, the French model is failing to deliver on its promise. France has 3.7m people living in poverty (defined as having a household income of less than half the median income); 2.5m living on the minimum wage; and over 2.4m unemployed.

Politicians will have to explain that tightening welfare rules need not rip a hole in the safety-net; that subjecting hypermarkets to more competition need not drive the *boulanger* or *patissier* from the high street; that removing pharmacists' monopoly on non-prescription drugs need not deprive every village of its green cross. They will also have to persuade voters that the prize is worth having. According to the IMF, more competition in French markets for both goods and services, combined with labour-market reform, could in the long run boost GDP by more than 10%.

The stakes are high. Next year's presidential and parliamentary elections will arguably be the most important for a generation. Unless Mr Chirac unexpectedly decides to stand again, they will bring an end to a stagnant 12-year presidency and provide a chance for a fresh start. France cannot afford to waste five more years.

This survey will identify the most urgent tasks that the new president will face and consider who is best placed to deal with them. The two presidential front-runners—Ségolène Royal on the left and Nicolas Sarkozy, currently the interior minister, on the right—are both in their early 50s, and both claim to offer a break with the past. But is this new generation as reform-minded as it sounds? And how can it build a consensus for change in a country that seems so resistant to being nudged out of its comfort zone?

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Insider and outsiders

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By trying to protect jobs and welfare benefits, France has created a two-class society

ON THE banks of the sleepy river Loire, across the valley from Amboise's historic *château royal*, stands a model of modern high-tech French manufacturing. In a neatly landscaped business park, Pfizer, an American pharmaceutical giant, produces 80% of the world's Viagra, and the entire supply for the American market. Every bottle of Viagra bought in an American drugstore will have been filled, packaged, labelled, bar-coded and shipped from this site. The Amboise factory manufactures Viagra in 227 different guises, from pill jars to blister packs. In all, the site turns out nearly 70m packs or bottles of pills of various kinds each year, labelled in 44 different languages.

Pfizer's Amboise plant shows that, for foreign investors, France remains an attractive location. This particular site offers a mix of high productivity, technical expertise (it has a big research facility, and nearby Tours is home to a pharmaceutical college) and reliability in a market troubled by fakes. Yet a visit to the gleaming, ultra-clean production line prompts another, more unsettling observation: there are hardly any workers.

No human being drives forklift trucks around the factory floors, fills pill packets or loads them into boxes. Instead, unmanned laser-guided vehicles surge down the aisles, picking up packages that have been stuffed, wrapped and labelled by machine, and delivered to the robots along conveyor belts suspended from the ceiling. All this takes place in an eerie near-silence. The factory's director, Marie-Gabrielle Laborde-Rayna, says that even visitors from the pharmaceutical industry familiar with high-tech production are impressed by the level of automation at Amboise.

A less comforting conclusion for the French, however, is that in France firms often invest in machines rather than hire people. This is not because French workers are inefficient. On the contrary, their productivity per hour worked is marginally higher than that of their American counterparts. It is, rather, because social-security contributions are high, the working week is short, the labour code is strict and shedding jobs is slow and difficult. Taking on an employee in France is a risk, so employers avoid it as best they can. This is the chief reason why France's jobless rate has been stuck around 8-10% for so long.

The current French model contains two chief weaknesses. One is this structural unemployment, which persists even in times of economic expansion. The second is the heavy weight of the public sector on the economy.

A two-tier market

First, unemployment. France's over-protected job market is well documented. In 2000-02, under a Socialist government, France shortened its standard working week from 39 to 35 hours without loss of pay. Although employers secured some flexibility in return, the new rules have caused headaches, particularly in the service sector. In order to spread the shorter hours over a year, many office workers get about three weeks of extra holiday, in addition to the normal five weeks of paid vacation, so companies have to juggle staff who are often away. Some bosses say it has encouraged absenteeism. Among local-government employees, for instance, this leapt by nearly 30% between 1998 and 2004. A flourishing service industry has sprung up to check whether people are away from their desks for a good reason.

Various other protections have built up over the years. National collective-bargaining agreements, which apply to all employees in an industry, whether unionised or not, entrench union power. The collective agreement for the hairdressing industry now runs

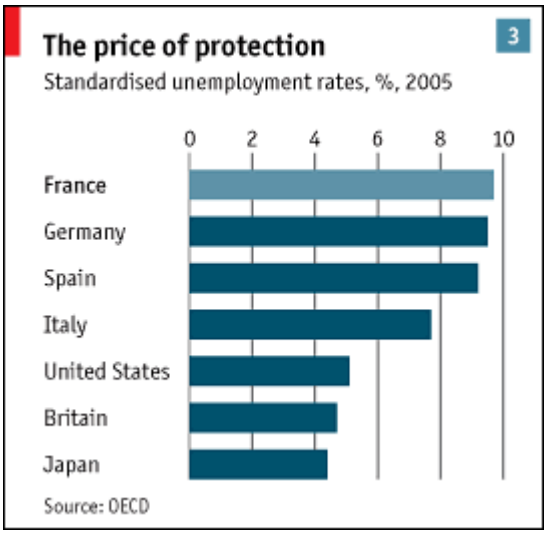
to a chunky 144 pages; the one for the bakery and patisserie industry goes on for an epic 480 pages. The general labour code this year is a veritable doorstop of 2,735 pages, 20% fatter than in 2000. Some of these rules protect the health and safety of workers, much the same as in any other Western democracy. But others add up to a bizarre effort to prevent people from working.

All this protection deters employers from creating permanent jobs in the first place. One fast-food boss says that in France his staffing levels per restaurant are only two-thirds of what they are in Britain. Many employers resort to temporary staff, interns or short-term contracts instead: precisely the sort of insecure work that the legislation set out to avoid. In the second quarter of 2006, two-thirds of net new private-sector jobs were of this nature. This has produced a two-tier labour market: good, protected jobs for some, and insecure jobs or unemployment for the rest.

The side-effect is felt not just by the outsiders—the young, the poorly skilled, the long-term jobless—but by the economy as a whole. Whereas France's big companies generally get by, its small companies struggle. Profits at the CAC 40 firms grew by 218% in the ten years to 2005, according to MEDEF, the employers' organisation; those at non-quoted companies by just 42% over the same period. Plenty of start-ups are launched in France each year but many fail to grow. Seven years after starting a business, says MEDEF, the average French entrepreneur employs only 7% more staff than he or she started with, compared with an extra 22% in Germany and 126% in America.

Some efforts have been made to lighten the burden on employers to encourage them to hire. Social-security contributions have been reduced for jobs paying the minimum wage and will be abolished altogether for minimum-wage jobs in firms with up to 20 employees. Jean-Louis Borloo, the jobs minister, has cut red tape and boosted tax credits for domestic-service jobs to increase the availability of help for the elderly, child-care and cleaning. The government has also brought in a new job contract for small firms that makes it easy to sack people for the first two years. The unemployment rate has now dipped to 9%, suggesting that the French labour market will respond to the right incentives.

Not enough people at work, not working enough: the result is an annual average rate of GDP growth in France that has been below the OECD average for the past ten years. If the French were working so little simply as a lifestyle choice, they might be happier about it. Yet as employers hold down earnings to accommodate the tighter rules, workers feel the squeeze in their wallets every month. Between 2000 and 2004 average net pay increased by just 1% in real terms. According to a government-commissioned report, if France had the same employment rate and working hours as Britain, its GDP would grow by an extra 20% over ten years.



The second main weakness of the current system is France's overweight public sector. As Michel Pébereau, chairman of BNP Paribas, a bank, put it in another report commissioned by the government that was published earlier this year: “For the past 25 years, every time a new problem has emerged, our country has responded by increasing spending.”

The instinct to meddle

Over that period, no government has presented a balanced budget. Public debt has grown to €1.1 trillion ($1.4 trillion), or 66% of GDP—five times its level in 1980. And this does not include France's off-balance-sheet civil-service pension liabilities.

Despite mini-reforms of the pension and health systems, the national audit office now says that the total social-security deficit is heading for over €37 billion by 2009. The reductions in the deficit that initially

followed these reforms were a “trompe l'oeil”. If nothing is done, Mr Pébereau forecasts that public debt will reach 100% of GDP by 2014 and 200% by 2032.

To support this spending habit, the state subjects its citizens to taxes and charges at every turn. Although income-tax rates are relatively moderate, especially for families, other imposts are heavy. An employer who pays a worker twice the minimum wage, or €2,400 a month, has to shell out nearly half as much again to the state in social-security contributions; the employee, for his part, has to hand over 22% of his pay in social-security contributions, on top of income tax. A French pay slip typically runs to over 40 itemised lines. Deductions from the employee's gross pay include 6.65% to the pension fund; 2.4% to the unemployment fund; and 5.1% to the social-security fund. The employer gets stung for contributions of 1.25% to the work-accident fund; 0.4% to the work medicine fund; 2.6% to the transport fund; and so on.

Were the state taxing the French in order to service debts incurred for long-term investment, it might all be more bearable. Yet the Pébereau report demonstrates the opposite: most borrowing pays for current operations, not research and development or higher education or infrastructure.

The result is an unsustainable administration. Over the past 20 years the state has hired nearly 1m extra civil servants, bringing France's total to 5m. In the Ministry of Agriculture alone, which serves an ever-shrinking number of farmers, the number of staff has grown by 8%. Yet the bureaucracy often does not provide good value for money. The country has a post office for every 3,530 inhabitants, twice as many as Germany, yet fewer of its letters arrive the next day. The Bank of France has 14,000 employees, even though French membership of the euro zone means it is no longer responsible for monetary policy—compared with 1,836 at the Bank of England, which retains that responsibility.

Too many layers of administration interfere too much in everybody's lives. The state sets the dates that shops can hold sales; forbids hypermarkets from selling below cost; limits the number of Paris taxis; and prevents pharmacists from owning more than one pharmacy. All the while, the lack of competition hampers growth and benefits producers. In the words of an official report into the lack of competition between hypermarkets: “Only one single market player has progressively lost out: the consumer.”

Back in 1856, Alexis de Tocqueville wrote about the country's “regulating, restrictive administration, which seeks to anticipate everything, take charge of everything, always knowing better than those it administers what is in their interests.” Nothing much seems to have changed. And nowhere are France's aspirations to excellence stifled more comprehensively by the weight of regulation than on the campuses of its universities.

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Lessons from the campus

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In higher education, a free-for-all does not work

EACH year, when Shanghai's Jiao Tong University publishes its world ranking of universities, France responds with a mix of indignation and consternation. Indignation, because French educators complain that the system favours “Anglo-Saxon” universities and makes no allowance for France's unusual division into elite *grandes écoles* and mass universities. Consternation, because not a single French university makes it into the world's top 40. Its best-placed institution—Paris VI—manages only 45th place.

France's university system encapsulates many of the drawbacks of its over-centralised, bureaucratic model. The country has 82 universities, catering to 1.5m students, twice the number of 25 years ago. All are public, and all the lecturers are civil servants. All the universities are barred from selecting undergraduates at entry. Enrolment fees amount to less than €200 a year, and all tuition is paid for by the state. Members of France's elite do their utmost to keep their children out of them and get them into the *grandes écoles*—for business, engineering or public administration—that cater to a lucky 4% of the student population.

Alamy

Toulouse I: cogito, ergo sum

To understand how France is tying its own hands with this system, consider two universities that lie just a few kilometres apart in the south-western city of Toulouse. Both are big: Toulouse I Sciences Sociales, a quick walk from the pink-brick Place du Capitole in the city centre, has 17,000 students; Toulouse II-Le Mirail, a short metro ride away on the city's outskirts, over 24,000. Both were spun off as separate universities after France's 1968 student riots, which led to the break-up of many of the country's giant universities. Both cover, broadly, the social sciences: Toulouse I offers economics, political science, law and management; Toulouse II-Le Mirail spans literature, philosophy, history, human sciences, arts and maths.

Toulouse II-Le Mirail, a low-rise 1960s campus of squat grey concrete blocks, looks like a demonstration model of most of France's difficulties with its university system. It has pockets of research excellence, such as in archaeology, and it has adapted to international standards by introducing the new Europe-wide bachelor and masters degree structure. But it concentrates on mass teaching in subjects—philosophy, psychology, sociology—that ill-prepare graduates for jobs.

Lecture halls are overcrowded. In one vast 800-seat amphitheatre, steeply banked rows of impassive students listen to a lecturer mumbling on a distant platform. Each year, 46% of all new students enrolled drop out. Daniel Filâtre, Toulouse II-Le Mirail's president, does not consider this to be his problem: “This is a left-wing university which has a social project,” he explains. “It is not an institution designed for professional training.”

Yet it is clearly a worry for the students. Fears about job insecurity prompted the countrywide university revolt earlier this year against Mr de Villepin's flexible contract for the under-26s. Two months of sit-ins, blockades and often violent skirmishes with riot police forced the prime minister to shelve his plan. But the malaise on French campuses such as Toulouse II-Le Mirail remains.

A generation ago most university graduates could have gone on to secure jobs in the public sector, often teaching the subjects they studied. Even today one startling poll suggested that three-quarters of French students would like to become civil servants. But the rapid expansion of numbers passing the school-leaving examination (*baccalauréat*)—from 25% of the relevant age group in 1980 to 62% today—has

flooded France's non-selective universities. Too many enrol in “soft” subjects rather than science or technology. Some 45,000 study a subject called “sports science”. Employers prefer to hire from vocational-training colleges. And sociology or psychology graduates often find their degrees worthless on the jobs market.

“Lots of students do want to become civil servants,” says Anna Mélin, a Toulouse student-union leader: “We're not adventurous because we are afraid.” Students worry about something the French call *déclassement*, meaning they have to accept jobs beneath the level they think their degree entitles them to. “Unemployment weighs on our minds,” says Ms Mélin. “We're the first generation that lives worse than our parents. Perhaps we in France have certain privileges, but I've no trouble admitting that we want to preserve them.”

In a bid to do so, student unions blockaded the campus at Le Mirail for two and a half months during the university sit-ins earlier this year. Graffiti sprayed on the walls linger: “We will strike against capitalism” and “We do not want to return to life as normal”. It is hard to find anybody satisfied with the way things are. Teachers are fed up because they are poorly paid and feel treated as second-class citizens. Students do not feel they get enough support. The 4,000 new undergraduates who arrive at Le Mirail each year get no tutorial support or careers advice. There is no bar on campus. The library is light, airy and brand new, but it closes at 6pm on weekdays and is shut at weekends.

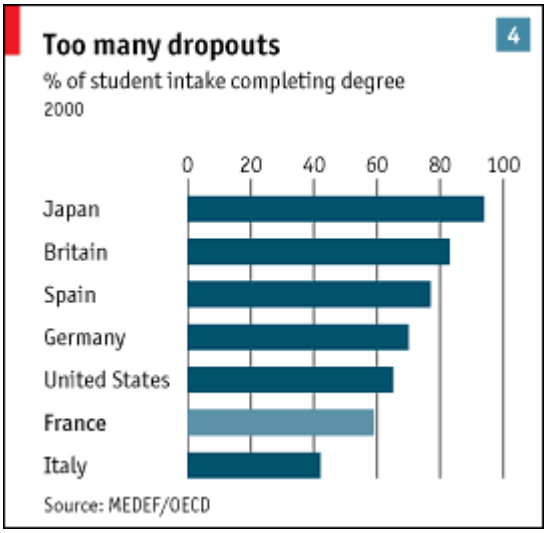
Across the Garonne

On the other side of the river, at Toulouse I, bicycles lean against red-brick courtyards and students sit cross-legged in the shade of plane trees. Toulouse I has not found a solution to all the difficulties Le Mirail faces. All the same, across all disciplines, 82% of third-year undergraduates there get their degree at their first attempt, compared with 58% at Toulouse II-Le Mirail. During the student revolt the Toulouse I campus was shut only for a brief period, and student leaders were booed.

It helps that the university has an international reputation for economics. It ranks fifth in the world for research in business economics, after the universities of Harvard, Berkeley, Chicago and Stanford, according to a global ranking. This autumn it launched the Toulouse School of Economics (TSE), which offers a two-year masters programme, taught entirely in English and designed for the international market.

In the 1980s Toulouse I was a social-science university much like any other, unable to select its staff or its students and squeezed for funds. Instead of accepting its lot, however, it decided to work around the rules. First, in order to help with finance, it sought private sponsorship for research. Various research centres were set up as associations, officially outside the university management structure and therefore not subject to civil-service rules. These were able to solicit research contracts directly with companies, such as France Telecom or Microsoft.

Second, it put research at the heart of the university structure. In general, universities in France concentrate on teaching, with research mostly organised by national public-research bodies. But international rankings put weight on research, which penalises the French. Toulouse I's Institute of Industrial Economics (IDEI), set up in 1990 by Jean-Jacques Laffont, a Harvard-trained economist, realised early on that it needed teachers and researchers to work and publish together in order to lift international rankings. This sounds simpler than it is. Even today, the institute's researchers are often employed not by the university but by the National Centre for Scientific Research—yet they also sign their papers in the university's name.



Third, Toulouse I has tried to get round the selection problem, though with greater success on the staff front than with undergraduates. It cannot refuse students who have the *baccalauréat*, so it gets plenty of mediocre ones in the early years. As for university staff, all posts are allocated by the Ministry of Education in Paris and recruited for nationally, through committees that include representatives of teachers' unions. Candidates for the most prestigious professorships are examined by a national jury, and universities with vacancies must accept

the jury's choices. To get round this absurd system, Toulouse I no longer directly recruits economics professors certified by the jury. Instead, it uses a transfer procedure to lure some of those who have taken up posts elsewhere.

The system can still defeat such efforts. Because lecturers are civil servants, academic appointments follow a calendar imposed by the Ministry of Education; job offers can be made only in the summer term. “But by then the international market has closed,” says Jacques Crémer, IDEI's director. “We lost a great candidate to the London School of Economics in January this year because he couldn't wait.” The struggle to stay competitive internationally, and to get round the system, requires heroic efforts—a huge waste of time and energy.

Reorganisation 101

The three watchwords for French universities are autonomy, competition and selection. First, if universities are to create centres of excellence they will need greater freedom: for example, to recruit their staff, to set up experimental links with research bodies or to increase enrolment fees. But before they can be granted such autonomy, their governing structures will need to become more effective and less beholden to unions.

Second, unless France embraces the idea of competition, the creed of egalitarianism will drag down quality for everybody. Part of the answer is more autonomy, to make experimentation possible. But it also requires a cultural shift. Does France want its best universities rewarded? Does it want them to compete for staff? Does it want to recognise that some universities are better than others? International league tables are prompting some change. To boost rankings, the government is creating “research poles” for universities and research centres to publish their findings jointly. It is also beginning to publish comparative graduation rates and job prospects for all universities.

This leads to the third problem: selection. The government hopes that by making such information public, it will deter would-be undergraduates from enrolling in dead-end subjects. For example, France currently has 65,000 psychology students—a quarter of the European total for that subject. Unless universities also get some say in whom they accept, such numbers are unlikely to fall much. And selection remains taboo. Could France ever allow universities to pick undergraduates at entry? “Oh là là!” replies a top education official. “It's not in the French mentality.”

But France does use selection for all its *grandes écoles*. Indeed, entrance exams to such places as Polytechnique and the Ecole des Mines (both engineering), Sciences-Po (political science), the Ecole Nationale d'Administration (public policy), HEC and ESSEC (business) are so stiff that they require two years' preparatory study. Such schools are regularly rated and ranked.

It is the *grandes écoles* that produce the well-polished graduates who get snapped up by companies in London or New York. And their alumni continue to hold power in France, in government as well as in the boardroom. Seven of the past 12 prime ministers, and two of the past three presidents, including both current incumbents, went to ENA. Some number-crunching done by *The Economist* for this survey shows that the grip of just two top schools—ENA and Polytechnique—on corporate France has actually increased over the past 20 years. When the CAC 40 index was created in 1987, 24% of the bosses of the companies it covered were graduates of one or other of those schools. By January this year that share had grown to 50%.

In reality, even the apparently non-selective universities apply a form of selection by quietly putting up with very high drop-out rates. But it comes after a huge waste of money and effort. “The French accept the brutality of selection on condition that we maintain the illusion of formal equality,” says Elie Cohen, an economist and member of the government's advisory Council of Economic Analysis. But on the face of it selection and competition are deemed to be bad for everybody—except the privileged ranks of a tiny elite.

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Reforming the unreformable

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From The Economist print edition

Some of France's big companies have shown the way

A FASHIONABLE subject for debate in recent years has been the question: “Is France reformable?” The implicit assertion is that it is not. The government capitulated to student protests. It has shied away from taking on such producer interests as teachers and train-drivers, electricity workers and hypermarkets. After nearly 12 years in office, President Chirac, for one, appears to have concluded that the French cannot take it. In a recent book, Franz-Olivier Giesbert, a journalist who has known Mr Chirac for over 20 years, writes that, traumatised by street revolts, the president “has ended up convinced that France is not able to tolerate any major reform”.

France, according to this argument, is inherently conservative and resistant to change. Some put this down to the system. Michel Crozier, a French sociologist, once described his country as a “blocked society”: too many top-down bureaucratic rules breed distrust among the people and create a system that can evolve only through crisis. Others suggest that the problem lies with the French themselves. In his 1976 book Alain Peyrefitte argued that France needed a “mental revolution” to alter its mindset in favour of risk-taking and innovation. Many French people seem to agree. Asked why reform in France is so difficult, respondents in a poll by LH2 in April this year said that the biggest single reason was “the state of mind of the French”.

Rex Features

The sunny side of globalisation

What seems to make reform especially hard is a peculiar French hostility to the market, the embrace of which is a precondition to many reforms. In a recent survey by Globescan, a polling group, 71% of Americans agreed that the free-market economy was the best system available, as did 66% of the British and 65% of the Germans. For France, the figure was 36%.

Some of this thinking seems to be taught at school. Of the three main *baccalauréat* options, one is a subject called “economic and social science”. Mr Cohen of the Council of Economic Analysis prefers to call it “a radical neo-Marxist amalgam of sociology and soft economics”. One widely used textbook devotes page after page to Marxist theories of production, class struggle and bourgeois exploitation. In a section on the labour market, it states that “employers seek to divide workers in order to reduce solidarity between different categories of staff.”

Perhaps such teaching helps to explain why the French gave a Trotskyite and a Revolutionary Communist 10% of the vote between them in the first round of the 2002 presidential election—and the Communist candidate another 3%. Marxist thinking still has a grip on the collective imagination. It comforts those at the bottom of the pile who rail at the recent explosion in executive pay, including some exorbitant corporate pay-offs. The 35-hour-week rules were based on the misapprehension that there is a fixed amount of work to be shared out. Nor is anti-liberalism a monopoly of the left. “Globalisation is not an ideal,” declared Mr de Villepin in his inaugural speech as prime minister last year. “It cannot be our destiny.”

But are the French really as anti-market as they profess to be? Consider Carrefour, a French hypermarket in Montesson, west of Paris. The store is vast, staff move around on rollerblades and shoppers can buy anything from mountain bikes to foie gras. Its shelves offer 14 different brands of washing powder, 12 of yogurt and eight of fresh fruit juice. The Tropicana brand alone, part of America's PepsiCo, is stocked in 18 different varieties, including ruby breakfast, sanguinello, mandarine-framboise, rouge plaisir, multivitamines, orange-mangue, pomme-litchi, réveil des tropiques and tonic breakfast, not to mention orange sans pulpe, orange avec pulpe, or even pulpissimo.

Watching French shoppers piling their trolleys high with such brands, it is hard to conclude that they are truly hostile to globalisation. In fact, many of the articles they so cheerfully consume are produced by their own companies, made rich by the system the French say they distrust. “I think we are totally capitalistic, but we just won't say so,” says Laurence Parisot, the head of MEDEF.

Don't mention the G-word

France's big world-class firms are as global as they come, striding into new markets from China to India and reaping record profits. Look at almost any industry and you will find a leading global French company: cars (Renault), tyres (Michelin), cement (Lafarge), drinks (Pernod-Ricard), insurance (AXA), food (Danone), cosmetics (L'Oréal), supermarkets (Carrefour), luxury goods (LVMH), and so on. Sodexho, a French catering company, even feeds the American army. As Claude Bébéar, chairman of AXA and head of Institut Montaigne, a think-tank, points out, such firms make about 80% of their profits outside France. They are daily proof of France's ability to benefit from globalisation.

AFP

Air France's Spinetta made it fly

Moreover, French employees within such firms have long learned to live by the rules of the global economy. Unionisation in France's private sector is low. In reality, France is divided: between those in the private sector who have long adapted to the market in their working lives, and those in the public sector who may accept globalisation as consumers in their free time but not while toiling at their desks.

But what happens to former public-sector workers whose enterprises have been privatised? Some of the most sclerotic formerly state-owned groups, icons of what the French call *immobilisme*, have been turned into competitive global enterprises. In the process, they have transformed work practices and staff attitudes. If this is possible, it suggests that the problem lies with institutions and the way change is managed, not some peculiar French conservative gene.

A good example is Air France. A decade ago the state-owned national airline was paralysed by bureaucracy and union-led resistance. Having teetered on the verge of bankruptcy, it was plagued by strikes and came to epitomise France's inefficient public sector. Yet today it is a profitable, competitive company. The French state's share in the company has shrunk to just 18.6%. Having merged with KLM, Air France is now Europe's biggest airline. In 2005-06 it made an operating profit of €936m, 69% up on the previous year.

“The idea of reform being impossible in France is contradicted by the facts,” says Jean-Cyril Spinetta, Air France's boss since 1997. Plainly, shareholder pressure after the company was floated helped to prompt change at the airline. Mr Spinetta has also taken some bold strategic gambles, such as the merger with KLM and an ambitious expansion of routes in the late 1990s. But a lot is also due to less tangible changes in the corporate culture.

In essence, Mr Spinetta inherited a distrustful, confrontational workplace and introduced some novel management tools: telling the truth, communicating with employees and explaining things. For instance, in the past, he says, good results were sometimes hidden from staff in case they triggered demands for pay increases. “The hardest thing was to get people to trust Air France,” he says.

Over time, Mr Spinetta earned credibility by keeping his word. When he faced fierce union hostility to privatisation, he promised there would be no redundancies, and made none. When unions claimed that

airline deregulation would destroy Air France, he insisted that it would instead bring opportunities, and was proved right. Having gained trust, he was able to push through reforms such as measuring productivity and introducing a service culture. His long tenure has also helped to bring stability. Since 2002 Air France has not had a single major strike.

Making mammoths dance

Other erstwhile fossils have been revived too, such as Renault, a carmaker that was near-bankrupt two decades ago, or Arcelor, a steelmaker recently snapped up by India's Mittal. Even Electricité de France, a fortress of communist-backed unionists, is quoted on the Paris bourse and sells electricity to Londoners.

What does this mean for French reform more broadly? The same principles apply. French politicians need to come clean about what needs to happen, and why. If they can win over public opinion, they will find it easier to face down those opposing change, whether they are public-sector unions or oligopolistic companies.

Unless France manages to introduce such reforms, its economy will struggle to recover, and any growth will be largely jobless. Failure will not only mean a lack of prosperity. It will also undermine the country's ability to face up to one of its biggest social challenges: the integration of its ethnic and religious minorities.

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Minority report

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The trouble with integration

CLICHY-SOUS-BOIS, where last year's riots started, is only 15km (9 miles) north-east of the tree-lined avenues of central Paris. To get there by public transport, though, takes nearly an hour and a half. The suburban RER train goes only to Le Raincy; then it is a slow, winding uphill bus ride to Clichy-sous-Bois. In less time, the high-speed TGV travels from Paris to Lille, 220km away. Ask locals in Clichy how often they travel to central Paris, and you draw a blank.

Reuters

Nothing better to do

A year ago, two youngsters were electrocuted in Clichy after climbing into an electricity sub-station, apparently while running away from the police. Their deaths triggered three weeks of rioting and car-burning in rough *banlieue* neighbourhoods across France, prompting the government to impose a state of emergency.

A year on, the place appears to be calmer. On a weekday after school, boys kick a football on a dusty patch of grass. Mothers, wrapped in bright green and ochre West African printed cloth, push buggies along the pavements. In an effort to improve its image, the town hall has organised a photographic exhibition about the suburb, called “Clichy sans Cliché”.

Yet a sense of isolation and abandonment hangs heavily in the air. One in five of Clichy's 28,300 residents is unemployed; on some housing estates the figure is half. Down the road from the halal “Beurger King Restaurant” (a play on the slang word for French-born Arab, *beur*), hooded youngsters of black African and North African origin hang out on the pavements. An upturned supermarket trolley lies in the alley between two tower blocks. In one 13-storey housing block, the lift is out of service for three weeks in four.

Over the years, Clichy's housing estates have become home to a mix of tongues, faiths and colours. The names engraved on the second-world-war memorial are Robert and Gabriel; those on the marriage bans posted outside the town hall are Rachida and Suleyman. In Clichy the disconnection from the capital is keenly felt. “I'm not Parisian, I'm from 9-3,” says one young man, referring to the department that covers the northern Paris *banlieues*.

Clichy has no police station, though one has been promised. When the police do appear, in vans, young men feel they are being picked on. “The police have a difficult time because innocent youths and criminal youths dress the same and speak the same,” says Claude Dilain, Clichy's Socialist mayor. “There's a

feeling that they are all hassled."

A different sort of uprising

When the riots started, they were treated in some quarters as a "suburban *intifada*". "*Jihad* comes home", ran one newspaper headline. Some American observers regarded the uprising as further proof of Europe's inability to control the spread of radical Islam. France has Europe's biggest Muslim population—an estimated 5m, or 8% of France's inhabitants—so it comes under special scrutiny.

A report into the riots by the French Renseignements Généraux, the domestic intelligence-gathering service, however, found the opposite. Islamists had "no role in setting off the violence or in fanning it," it concluded. Clichy's mayor agrees. "I completely reject the idea that the riots were an Islamist plot," he says. "During the rioting I never heard of a young man burning a car in the name of Allah; but I heard of plenty of Muslims saying, 'go home in the name of Allah'."

Instead, the intelligence officers reckoned, the rioting was a "popular revolt" provoked by a toxic concentration of social problems: joblessness, poverty, illegal immigration, organised crime, family breakdown and a lack of parental authority. France had been so preoccupied with watching Islamic radicals, said the report, that it had neglected the wider problems in its *banlieues*. On certain housing estates, adds Alain Bauer, a criminologist, organised criminal gangs, shaken by recent police raids, took advantage of the uprising. By first encouraging and then calming the rioters, he says, the gangs tried to remind the police of their power.

"The problem is not Islam", says Olivier Roy, an Islamic scholar, "but integration." France clearly has no monopoly on a ghettoised, isolated underclass, but the lack of work makes integration in its *banlieues* particularly difficult. "The only integration that means anything is a job," says Samir Mihi, a youth worker at Clichy's town hall whose parents are from Algeria.

Clichy has no government-run job centre, so the jobless have to catch a bus to a neighbouring suburb to peruse job vacancies and talk to a job-placement adviser. Many of those who make the effort say that their applications get nowhere; they suspect that a foreign-sounding name, or the local postcode, puts employers off. An experiment by the University of Paris I, using identical CVs, showed that a white-sounding French name produced five times as many invitations to an interview as a North African name. There is racial discrimination on an "undreamed-of scale", said the Institut Montaigne in a landmark 2004 report.

Because of the relative lack of social mobility out of France's *banlieues*, the multi-ethnic nature of the French population is not reflected at the top—other than in sport and popular culture. The French establishment is dominated by white men. There is not a single member of parliament of non-white immigrant origin representing mainland France. There are only two prefects and hardly any mayors. "Where is the French Condoleezza Rice or Colin Powell?" asked Mr Sarkozy, who advocates affirmative action, on a recent trip to America. When Harry Roselmack, a black Frenchman, was selected this summer as evening news anchor on France's top TV channel, TF1, his face was splashed across the front pages.

How French can you get?

France's integrationist doctrine firmly rejects official recognition of separate communities. In the past this has helped to mould generations of foreigners—Italians, Poles, Portuguese—into Frenchmen. But the children of later inflows—Algerians and Moroccans, then Malians, Ivorians and Senegalese—have found it more difficult to fit in. The persistence of a large jobless multi-ethnic underclass, combined with the dearth of non-white faces in top jobs, mocks France's claim to be colourblind. "Under the cover of an abstract concept of 'equality'," says Mr Baverez, the author, French society "practises a pitiless form of apartheid".

Does this mean that the French integration model has failed? Not necessarily. Indeed, in the wake of the London terrorist attacks in July 2005, some British multiculturalists who once castigated the French for banning the Muslim headscarf in state schools are looking with fresh interest at France's way of instilling a sense of citizenship. The French

AFP

approach does have its strengths. France has an unapologetic sense of national identity, taught to every child at primary school. The *tricolore* flag flutters outside every town hall. Official documents are available only in French, and the language is regarded as a passport to integration. After a bloody struggle against authoritarian Catholicism, church and state were separated in 1905 and religion firmly banished to the private sphere; the French have bent over backwards ever since to keep it there, under a version of secularism they call *laïcité*.

This unambiguous, well-articulated sense of nationhood seems to rub off on its newer citizens. A recent study by the Pew Centre showed that, whereas 81% of British Muslims considered themselves to be more Muslim than British, only 46% of French Muslims considered themselves to be more Muslim than French.

The exceptional Roselmack

The challenge for France is to put sufficient trust in the strengths of its republican system to deal with its weaknesses. For example, it could introduce some sort of affirmative action without embracing multiculturalism wholesale. Two of the *grandes écoles*, Sciences-Po and ESSEC, have experimented with special admission for students from the *banlieues*, chiefly by setting up links to schools there, with great success. Neither has resorted to quotas, nor to labelling ethnic minorities, which France resists so strongly.

France cannot treat the problems in the *banlieues* merely as a security issue. For sure, on the worst estates crime continues daily, and is often violent. But the only real solution is to build ladders out of the *banlieues*, with jobs at the end of them. “Unemployment destroys all social models,” says Louis Schweitzer, former CEO of Renault and head of France's new anti-discrimination body.

France's riots may not have been about Islamic radicalism, but that does not mean that France is sheltered from militant Islam, nor from Islamist terrorism. The *banlieues* are fertile ground for recruitment. Of the 1,600 mosques in France only about 50 are considered militant. Yet they toil efficiently to win the minds of the young, jobless and disaffected.

Security matters

The country's robust surveillance regime, combined with extensive judicial counter-terrorism powers, enables it to keep a close watch on Islamist activity. Mr Sarkozy does not hesitate to expel militant clerics. In France, suspects can be charged simply for “association” with those plotting terrorist attacks.

Two routes to radicalisation are of particular concern, though. One is conversion: there are thought to be 30,000-50,000 Muslims in France who have embraced the religion only in recent years. A small number are among France's most virulent Islamists, such as Pierre Robert, alias “Yacoub”, who is currently serving time in Morocco for the 2003 terrorist attack in Casablanca.

The other route is proselytising in prison. Well over half of France's inmates are Muslim, and radicals find jail a fruitful place to spread their message. Overall, French counter-terrorism authorities have identified a hard core of 50-100 would-be terrorists, provided with moral and material support by a few hundred others.

Security operations aside, France has also made an effort to temper militant Muslim groups through co-option. In 2003, despite its secular status, it took the unusual step of setting up a religious body, the French Council of the Muslim Faith. It was put in the moderate hands of Dalil Boubakeur, rector of the Paris Mosque, but included some hardline groups.

The council has struggled to earn credibility. The real hardliners—the Tabligh, or Salafists—lurk way beyond its reach. And it has been beset by political infighting at national level. Yet it has been useful in some ways. Even its more militant leaders, for instance, condemned hostage-takers in Iraq who demanded that France repeal its headscarf ban.

All the same, nobody is suggesting that France has solved the challenge of Islamic radicalisation. Indeed, the country is keenly aware that it has recently been named a target by al-Qaeda. Moreover, the recent French decision to send peacekeeping troops to Lebanon is viewed with some unease. For the way France

handles its Muslim minority at home is linked with its relations with Muslim states abroad.

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Beyond these shores

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France's foreign relations need a rethink

AT THE height of the recent Israel-Hizbullah conflict, France found itself at the forefront of world diplomacy for the first time since the start of the war in Iraq. Ministers were dispatched to Beirut, diplomats to America. The phone line buzzed between Jacques Chirac and George Bush. Best of all, the French persuaded the Americans to wait for a ceasefire and a political agreement before sending a multilateral peacekeeping force—an achievement that was hailed in Paris as a victory for French diplomacy.

AFP

Thin on the ground in Lebanon

And then France wobbled. Its initial contribution was a mere 200 soldiers. Only after it was upstaged by Italy's muscular offer of 3,000 troops did it boost its own numbers to 2,000.

The episode exposed both the aspirations and the limitations of French diplomacy. France, Lebanon's former colonial administrator, felt gratified to be asked by America and Europe to take a lead. This reaffirmed its status as a world power at a time when it had been struggling to make its voice heard. And it seemed to legitimise its strategic value in the Middle East as an independent-minded alternative to the Anglo-American axis.

Yet France's wavering also betrayed the limits to those ambitions. The French seemed happier to send their men to the negotiating table than to the front line. In fact, France's army was already stretched overseas. Thanks to recent increases, the French defence budget now runs to 1.7% of GDP, according to France's defence ministry, but that is still well below Britain's 2.2%. And France was nervous about committing soldiers to a place that has proved lethal in the past, and in the Islamic world when its own Muslims are restless.

France saved its credibility just in time. But if it wants to retain global influence, it now needs to attend to the weaknesses in two key foreign-policy relationships: its transatlantic ties and Europe. France may still hold sway over the French-speaking world, but that will count for little unless France repairs those two links.

In American eyes, France has still not recovered from the 2003 fall-out over Iraq and Mr Chirac's threat to veto a UN military force. “France can plead all it wants for the Americans not to strike Iran,” says François Heisbourg, of the Foundation for Strategic Research, a think-tank. “But they will not listen, because France has no credibility there.”

At the same time, France's rejection of the European constitution has put matters in Europe on hold too. France has yet to work out what it now wants from Europe, or how it can hope to get it. The French sense this unease: about 60% think that France's role in the world is weakening, according to a poll by TNS-Sofres.

Burying differences

Last month Mr Sarkozy went to America to launch a charm offensive and tell his hosts it was time to turn the page on Franco-American disagreements. Under a big blue sky in New York, he commemorated the terrorist attacks of September 11th 2001, decorated the city's police chief and firemen, remembered the victims at a church service and promised that “we haven't forgotten, and we'll never forget.”

There are, broadly, two versions of what needs to be done about Franco-American relations. One, advocated both by the Socialists and by Mr Chirac, argues for sticking to France's neo-Gaullist independence. The other is the Atlanticist solution so prominently displayed by Mr Sarkozy during his recent trip.

The boldest exponents of these two contrasting views are, respectively, Mr Chirac and Mr Sarkozy. Mr Chirac believes in building up Europe to counterbalance American power, and will not contemplate a “relationship of submission” to America; Mr Sarkozy believes it is “unthinkable for Europe to forge its identity in opposition to the United States”. Mr Chirac threatened to veto UN intervention in Iraq; Mr Sarkozy was also against the war, but says that France diminished its influence through “arrogance”.

Their divergent transatlantic reflexes shape their thinking on Africa and the Middle East too. Mr Chirac has close personal ties to African leaders; Mr Sarkozy wants to sweep aside “the old-time networks”. Mr Chirac does not consider Hizbullah a terrorist organisation; Mr Sarkozy says it is. Mr Chirac calls Iran “an old civilisation, a great country” which should be respected; Mr Sarkozy says it is an “outlaw nation” and that, in dealing with it, “we must leave all options open.” Mr Chirac has traditionally been cool towards Israel; Mr Sarkozy is instinctively sympathetic. “He makes Americans feel comfortable with Frenchmen,” commented Israel Singer, of America's World Jewish Congress, after a private meeting between him and Jewish leaders in New York.

The Socialists, for their part, have been latently anti-American since the 1950s, when the French left was seduced by communism. The Socialist Party campaigned for the European constitution with the slogan “A strong Europe to face up to the USA”. Ségolène Royal talks about the need to counterbalance “the American hyperpower”.

Certainly the Socialists too want to restore trust to the transatlantic link; but they are unsparing in their criticism of Tony Blair toeing the American line over Iraq. After Mr Sarkozy's American jaunt, Laurent Fabius, a former prime minister and candidate for the party's presidential nomination, sneered that the interior minister would be “the future poodle of the American president”.

One thing is sure: France needs to find a better way to deal with disagreements with America. Mr Sarkozy may be right in saying that the tone of France's opposition to the Iraq war was ill-judged: “It's not appropriate to try to embarrass one's allies.” Any real improvement may have to wait for the departure of the two countries' respective presidents, between whom no love is lost. Mr Sarkozy also has a point when he says that the French in general, who devour American popular culture, are far less anti-American than their elites.

The bigger question is how well France's interest would be served by a strategic Atlanticist shift. Taken to extremes, this would challenge a French diplomatic tradition dating back to the time when Charles de Gaulle pulled France out of NATO's military command in 1966 and American soldiers quit French soil. France may not be listened to in America just now. Yet it seems that loyal friends such as Mr Blair are not always listened to either.

France has its uses

Prickly, independent-minded France may exasperate the Americans at times, but even within the Western alliance it can sometimes be useful to have one power that speaks its mind. Who else was pointing out to America the post-war risks in Iraq, as Mr de Villepin far-sightedly did in his 2003 speech

to the UN? The Americans may still resent the tone of that admonishment, but they and the British recognise the value of France's credibility in the Arab world—and sometimes draw on it to everybody's benefit. In short, France will have to steer a careful course between rebuilding trust sufficiently to strengthen its influence and retaining its ability to speak out.

Getty Images

Sarkozy cosied up to Bush

Just as France needs to work on its transatlantic links, it needs to boost its credibility in Europe. The French rejection of the proposed EU constitution knocked the political class sideways. Although polls had predicted a “no” for weeks before last year's vote, nobody could quite believe that the French, of all people, would turn their backs on a constitution that entrenched European integration. Since then, French policymaking in this area has been blocked.

In the post-war era France's foreign policy has been built around the idea that, as a medium-sized ex-colonial power, it would do best to project its voice and further its ambitions through a Europe created to its design. EU enlargement to 25 members in 2004 put an end to this, shifting Europe's centre of gravity to the east and diluting France's influence. The French referendum result was a belated cry of popular protest: against a Europe France no longer recognised, a project it no longer dominated, an organisation that seemed to be more about free markets than political ambition.

Both the French left and right still agree on the need for a strong political Europe. Even Mr Fabius, who broke ranks with his own party to campaign against the constitution, was protesting against what he saw as an excess of economic liberalism in Europe, not against European integration. Now both the Socialists and Mr Sarkozy want a new slimline treaty that would introduce institutional changes to make the enlarged union work better.

The trouble is that France has not yet devised a foreign-policy framework that would enable it to achieve these ends. As for a mini-treaty, it will struggle to get a document to its liking. Many of the elements that it wants will be firmly resisted not only by the British but also by others, such as the Germans and the Poles. The British would contest, for instance, any French attempt to extend qualified majority voting to areas such as taxation, or to shut the door to Turkish membership, both of which Mr Sarkozy advocates.

That said, France is not condemned to being marginalised in Europe. As Lebanon shows, its military force gives it a pivotal role in foreign affairs in Europe. France will need to invest more in troops and hardware if it is to continue to take part in global policing and make diplomatic use of its military might.

France also needs to work out how to build the alliances in an enlarged Europe that would enable it to press its case. This means reaching out to new members, not snubbing them. Few have forgotten Mr Chirac's dismissal of them as “badly brought up”. And the smaller countries are nervous about Mr Sarkozy's talk of a “big six”—France, Germany, Britain, Spain, Italy and Poland—which he sees as an informal platform for reconciling differences, not unlike the Franco-German axis in an earlier, smaller EU. Mr Sarkozy may argue that the Franco-German compact is passé, but France will have to work closely with Germany to try to maintain some influence in Russia and its regional neighbours.

Blame it on Europe

At heart, the French are sceptical about what Europe can do for them today. They are hostile to Turkish entry. They think that open markets are a menace to French jobs and companies. They talk a lot about the need for Europe to be closer to the people, more open, more visible, more relevant, in order to be loved again. All of which may be right. But what is needed most of all is a big effort by French politicians. For years, they have conveniently blamed Europe for many of the uncomfortable changes that they themselves have introduced. And they have kept on talking extravagantly about French *grandeur* even as France's voice was waning. The cumulative effect has been to undermine Europe in the eyes of the French electorate.

Where is the politician who explains how French companies have benefited from the opening up of markets in eastern Europe? Where is the politician who has faced up to France's diminished voice, and

put forward a plan to strengthen it again? Unless French leaders are prepared to be straight with their voters, they will damage their credibility and their influence—not only abroad but at home too.

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Where there's a will

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From The Economist print edition

Next year's elections offer France the chance of a fresh start. But which candidate to vote for?

NICOLAS SARKOZY appears to be asleep. Perhaps that should not be surprising. As the head of the governing party, the Union for a Popular Movement (UMP), number two in the government and would-be presidential candidate, he has a hectic schedule, and is resting aboard a flight in America between visits to Brussels and London. But Mr Sarkozy's public image is one of such frenetic activity that it comes as a shock to discover even he can come to a standstill.

If precedent alone governed French voting behaviour, the Socialist Party ought to win next year's elections hands down. The centre-right UMP is unpopular in government. After nearly 12 years in power, Mr Chirac has worn his credibility to a thread. For the past 28 years, the French have not once re-elected an incumbent government. By voting Mr Le Pen into the 2002 presidential run-off and rejecting the EU constitution, the French have demonstrated their ability to cause trouble through the ballot box.

EPA

Evergreen Le Pen

Yet Mr Sarkozy may have managed to upset these electoral rules. Despite a career in politics spanning nearly 30 years, and despite his service in Mr Chirac's present government, he has somehow persuaded public opinion that he is a gust of fresh air, ready to bring about a “rupture” with the Chiraco-Gaullist past. France, he argues, “has to face up to the truth and stop deluding itself”: nothing short of an overhaul of the French model will rescue it from continuous decline.

Mr Sarkozy's poll numbers suggest that voters believe him. He remains the overwhelming favourite on the right, with a popularity rating of 50%, compared with just 29% for Mr de Villepin, the prime minister. By constantly defying the president and grabbing control of the party Mr Chirac founded, Mr Sarkozy has distanced himself from the government he serves. Assuming he wins the UMP's nomination in January, the Socialists cannot be sure of victory, even if they pick the one candidate—Ségolène Royal—who opinion polls suggest could beat him.

When the French cast their ballots next April and May, they will face an embarrassment of contenders who will fragment the vote. The left may be split by the Communist Party, under Marie-Georges Buffet, and the Greens, under Dominique Voynet, along with one or more ultra-left anti-liberal candidates. The centre-right vote may be eaten into by François Bayrou, leader of the Union for French Democracy. On the far-right fringe Mr Le Pen is enjoying a resurgence, opening up the possibility of a repeat of 2002, when he beat the Socialists and made it to the run-off. The chances of this happening will be greater, according to recent polls, if any candidate other than Ms Royal wins the Socialist nomination. Two others are standing: Laurent Fabius, an ex-prime minister, and Dominique Strauss-Kahn, an ex-finance minister.

If, on the other hand, Mr Sarkozy and Ms Royal turn out to be their parties' respective nominees, and polls stay where they are today, the pair should make it through to the run-off. At that point it will be a tight contest, dividing France down the middle. The choice this time matters more than it has done for a long while. “It will be one of the last occasions for France to carry out reform peacefully,” argues Mr Baverez, the political author.

Over the past year, the battle for public opinion between Mr Sarkozy and Ms Royal has injected an

element of American-style show business into staid French politics. They are both in their early 50s, born into the television age and fast converts to the power of the internet. Stolen paparazzi snaps—on the beach, with the family—lend a celebrity aura to the contest. In the short run the election of either of them would instantly lift the public mood.

With a return of confidence, the parliamentary elections that follow the presidential poll are likely to produce a matching majority. But the French specialise in staging rebellions through the ballot box. “Cohabitation” between a president and a government of differing political colours cannot be ruled out, and would paralyse policymaking.

The language of change

Will anybody seize a change of mood to pursue bold reform? Mr Sarkozy comes the closest to talking the language. “The French aren't afraid of change,” he claims, “they are waiting for it.” He argues that, by explaining the need for reform in simple everyday language, he can win over public opinion and face down vested interests. To this end he favours a blitz of legislation early in a mandate, while public opinion is in favour of change.

Much of Mr Sarkozy's confidence stems from his belief in his own powers of persuasion. Sometimes he uses them skilfully; at other times he is heavy-handed. When, as finance minister in 2004, he wanted to see lower prices in French hypermarkets, for instance, he summoned the grocery bosses and told them to do as he said, or he would “out” them in the press. He likes nothing more than taking on vested interests—whether judges or railwaymen—by appealing to public opinion. He would be far less beholden to public-sector unions than the Socialist Party. That would give him more freedom to streamline the civil service and to reform the special public-sector pension regimes, both of which he has promised to do.

But Mr Sarkozy is far less convincing on industrial policy or farm support. He was unapologetic about using public money to rescue Alstom, an engineering firm, or defending a Franco-German pharmaceutical company, Aventis, from a hostile foreign bid by arranging an alternative merger with a French firm, Sanofi. It is not clear that he really believes in letting the market decide. The French may consider him to be an economic liberal, but he is ambivalent about the label. “I don't wake up every morning asking what Hayek or Adam Smith would have done,” he says.

His detractors may call it incoherence, but Mr Sarkozy describes it as pragmatism. “I do what works,” he says. In many ways, he shares this attribute with Ms Royal. Both belong to a post-ideological political era, liberally borrowing ideas from the rival side and resisting doctrinal constraints. Mr Sarkozy says that he would introduce positive discrimination to promote ethnic minorities, and give foreigners from outside the EU the vote in local elections. Ms Royal, the daughter of a colonel, says that she would send young criminal offenders from the *banlieues* for military training to learn discipline. To the consternation of fellow Socialists, she admires Britain's Tony Blair; she talks about the need to restore the value of work, and to “reconcile the French with business”.

The pair share other characteristics too. Both have persuaded voters that they are fresh, even though they have been in politics for decades. And although both define themselves as outsiders, they are stretching the point. Mr Sarkozy may be the son of an immigrant, as he often points out, but his father was a Hungarian aristocrat, and he was raised in, and elected mayor of, the swanky Paris suburb of Neuilly. For her part, Ms Royal is a graduate of ENA, the elite postgraduate civil-service college; she worked for years at the Elysée Palace as an adviser to François Mitterrand; and her partner, François Hollande, happens to be the leader of the Socialist Party.

On balance, however, the two front-runners occupy quite different political positions. By and large Mr Sarkozy's ideas place him to the right, and not only on immigration and criminal justice. He is in favour of loosening redundancy rules, penalising those on welfare who refuse jobs or training and introducing a pay-as-you-earn income-tax system.

GOFF

Those who know Ms Royal well say that on economic policy she remains to the left. She has tied public aid for firms in the Poitou-Charentes region, of which she is the elected president, to the creation of secure, well-protected jobs. In speeches she talks in neo-Marxist terminology about the relationship between capital and

labour. She denounced the 35-hour week not because it was a burden on employers but because it enabled them to extract concessions from workers.

Ms Royal's candidacy is not guaranteed. Ahead of the party's election, her rivals have been manoeuvring hard to thwart her victory. An anti-Ségolène alliance could give her a tough second-round ride. But whichever candidate they pick, the Socialists are likely to stand on a resolutely left-wing programme, which would lean towards protecting the existing model rather than reforming it.

Royal progress

Expect some surprises

There are two caveats, however, to the idea that Mr Sarkozy would be a more determined reformer than any candidate on the left. The first is that, in power, the Socialists have often turned out to be less left-leaning than they appear on the campaign trail. It was Lionel Jospin, for instance, who as prime minister floated such former state treasures as Air France, France Telecom and Aerospatiale. If a relative moderate such as Mr Strauss-Kahn became prime minister, he might resist the wilder elements of the party programme.

The second caveat is that Mr Sarkozy himself, if elected, might turn out somewhat less bold than expected. How long would he hold out against strikes and unrest on the streets? After all, previous would-be reformers also promised to change France, only to give up in the face of hostility. Listen to Mr Chirac 12 years ago: “Either the French give in to the temptation of conservatism, and the worst is to be feared,” he argued, “or our compatriots choose hope, and thus change, and France will remain a unified, prosperous, peaceful country and respected in the world.” Fine words, but they did not last.

Next year offers the chance of a fresh start. The French may be in a glum, restless mood, as the British were in the 1970s. But they are also readier to change their ways than their traditional elites suggest. It all depends whether political leaders are ready to be frank with them about the need for change, and courageous enough to implement it.

Back in 1979, a British opposition leader, lamenting the country's “national decline”, voiced admiration for the way in which a fellow European country had transformed itself, demonstrating that “given the will, the policies, the leadership, a country can pull itself up by its own bootstraps to the lasting benefit of all its people.” The opposition leader in question was Margaret Thatcher. And the country she admired was France.

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Nintendo

Playing a different game

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Does Nintendo's radical new strategy represent the future of gaming?

AP

IF TALK of synergistic processing elements, parallel floating-point shader pipelines, vector units and 1080p high-definition video sets your pulse racing, you are probably looking forward to the launch of the PlayStation 3 (PS3), Sony's new video-game console, which goes on sale in Japan and America next month.

Most people find such technical trivia baffling, however. As a result, the video-games industry's relentless pursuit of ever more computing power and graphical detail might ultimately prove counterproductive. That is the view of Satoru Iwata (pictured), the president of Nintendo, the Japanese company that dominated video-gaming in the 1980s before being deposed by Sony. Its new console, called the Wii, is also launched next month. But it is a very different beast from the PS3, inspired by a radically different strategy.

Video gaming is a cyclical industry in which new consoles are launched every five or six years. In the last cycle, which began in 2000, Sony's PlayStation 2 emerged as the clear victor, far outselling Microsoft's Xbox and Nintendo's GameCube. The next cycle will pitch Microsoft's Xbox 360, launched last year, against the PS3 and the Wii. With each cycle the power of the hardware increases, making possible better graphics and more complex games. But Mr Iwata believes the industry has reached a crossroads: by designing products for existing gamers and neglecting non-gamers, it undermines the prospects for future growth. There have even been signs in Japan that the market was starting to shrink. “We need something radical to change the situation,” says Mr Iwata.

The main problem with modern games, he says, is that they require players to invest enormous amounts of time. As lifestyles have become busier, leaving less time for gaming, the industry has moved towards epic games which take dozens of hours to complete. This is leading some occasional gamers to stop playing and deterring non-gamers from giving it a try, says Mr Iwata. There are other factors too: novices are put off by the need to master complex controllers, festooned with buttons, triggers and joysticks. And not everyone wants to escape into a fantasy gaming world. “That attracts avid gamers,” he says, but can make it “difficult for people to become interested in games”.

Nintendo set out to reach beyond existing gamers and expand the market. This would involve simpler games that could be played for a few minutes at a time and would appeal to non-gamers or casual gamers (who play simple games on the web but would not dream of buying a console). They would be based on new, easy-to-use controls. And they would rely on real-life rather than escapist scenarios. This was not an entirely new approach: dancing games that use cameras or dance mats as controllers have proved popular in recent years. But Nintendo began to design entire games consoles around such ideas.

The testing-ground for Nintendo's new strategy was the DS, a handheld console launched in 2004. It has two screens, one of which is touch-sensitive and can be tapped or written on with fingernails or a stylus. This made possible games that did not rely on complicated combinations of buttons. “We didn't know, if the DS didn't make it, what kind of products would be needed,” says Mr Iwata. But in the event the DS was a smash hit and has sold more than 21m units worldwide. This month Nintendo raised its profit forecast for the current year because of unexpectedly strong sales of DS consoles and software.

The most popular DS game is “Nintendogs”, in which the player takes dogs for walks, teaches them tricks and enters them in competitions. The dogs can be taught to respond to voice commands issued via the DS's built-in microphone and petted via the touch screen. “Nintendogs” has proved particularly popular with female players. Also successful are the “Brain Training” games, which consist of puzzles designed to keep the player's brain young and nimble. Unlike most games, which sell well for a few weeks before sales tail off, “Brain Training” sold consistently for months, and Nintendo's research found that 60% of sales in Japan were to new users who bought DS consoles specifically to play it. Just as “Nintendogs” appealed to female gamers, “Brain Training” has helped to bring gaming to an older audience.

The Wii is an attempt to apply the lessons of the DS to a fixed console that plugs into the television. Its key innovation is its wand-like controller, which resembles a simplified TV remote-control rather than the usual button-strewn joypad. Motion detectors translate the movement of the wand into on-screen action, making possible tennis, fishing and sword-fighting games. (Some games use an add-on controller held in the other hand.) The Wii can also display news and weather information from the internet, organised alongside the games as a series of “channels”. Old games from Nintendo's back catalogue can be downloaded to draw in lapsed gamers.

This is, admittedly, a harder sell than the DS, says Mr Iwata, since a portable console lends itself to word-of-mouth promotion. His hope is that existing gamers will act as ambassadors, encouraging friends and family to give the Wii a try. And by providing non-gaming functions such as news and weather too, the aim is to overcome non-gamers' aversion to consoles, so that eventually they might flick to the “games” channel and give something a try.

The contrast with Sony is striking. It is pushing the PS3 as the most advanced console, with a powerful new processor chip and a high-definition “Blu-ray” optical drive. But its complexity has so far proved a liability rather than an asset, pushing up its price (to $500, compared with $249 for the Wii) and delaying its launch by several months. The PS3 will not appear in Europe until next March, and the console will be in very short supply for months. This week Sony said its profits in the latest quarter had been wiped out by PS3 problems and a massive recall of faulty batteries supplied to other computer-makers. This has dented Sony's reputation just as it is trying to emphasise its technical prowess.

The industry had been preparing for a showdown between Sony, the current champion, and Microsoft, its deep-pocketed challenger. Nintendo was expected to be an also-ran, peddling its familiar game brands, such as Mario and Zelda, to children and die-hard fans. But its unusual new strategy means that Nintendo is now the company to watch. As it sets out to broaden the gaming population, Nintendo is not fighting against Sony and Microsoft, says Mr Iwata. Its real enemy is the indifference that many people still feel towards gaming. Of course, says Mr Iwata, he would be happy if Nintendo became the leading console-maker again as a result of its new approach. But a victory over Sony and Microsoft in a shrinking market, he says, would not be a victory at all.

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Tata and Corus

Steely logic

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Why the Tata-Corus deal makes sense for both parties

IN THE early 1900s, when Britain ruled India, the chairman of the colony's Railway Board, Sir Frederick Upcott, was so sceptical about Tata, then a young steel company, that he declared he would “eat every pound of steel rail” that it could produce to Britain's exacting specifications. His subsequent indigestion is not recorded, even though Tata was producing hundreds of tonnes a year by 1916. Similar scepticism would have been justified if anyone had suggested two or three years ago that Corus, the Anglo-Dutch steelmaker which includes the once-mighty British Steel, would receive a takeover bid from Tata Steel, a much smaller Indian firm. Yet that is what happened on October 20th when Corus accepted an $8.1 billion takeover bid from Tata to form the world's fifth-largest steel producer.

AFP

Tata and Leng's Corus of approval

When Jim Leng, Corus's chairman, began making foreign forays a year or so ago to find low-cost sources of steel slabs for his European steel-finishing plants, Tata was one of his first ports of call. He also talked to O.P. Jindal, a smaller Indian steel group, and to firms in other countries. But as steel prices hardened this year, Corus switched from being a steel buyer to a takeover target, and the cash-rich Tata group saw the opportunity to achieve global scale a few months after Mittal Steel, run by Lakshmi Mittal, an Indian-born businessman based in London, had swallowed Arcelor, a European steel company. The aim, says Ratan Tata, who heads the group, was not just to increase Tata Steel's size, but also to achieve a “strategic fit”.

The Arcelor-Mittal deal, plus plans by Mr Mittal, POSCO of Korea, and others to set up integrated iron-and-steel plants in India, had made Tata Steel feel vulnerable. In the past decade, Tata has updated its technology and slimmed down its workforce to become one of the world's lowest-cost producers. But it is still small, with only 5.3m tonnes per annum (mtpa) steel output, compared with Corus's 18.2mtpa and Arcelor-Mittal's 109.7mtpa. It plans to spend some $15 billion to build three integrated iron-ore mining and steelworks in the Indian states of Orissa, Jharkhand and Chattisgarh. That will add 23mtpa in capacity, but will take 10-15 years.

In the meantime, Tata has been expanding abroad. It acquired Singapore's NatSteel in 2004 and Thailand's Millennium Steel last year, which together added about 4mtpa. It also bid for South Africa's Highveld Steel, and will bid again if Evraz of Russia does not complete its agreed takeover of the firm. And it has plans for big iron-ore and steel projects in Iran and Bangladesh, though both are currently on hold for political reasons.

All of these moves are the result of a strategy introduced three years ago by B. Muthuraman, Tata Steel's managing director. Tata, which mines all the iron ore and coal it needs, now aims to carry out primary steel production close to its iron-ore deposits, and then ship semi-finished steel for finishing close to foreign consumer markets. This meets demands from Indian states that they should have the benefit of adding some value after their iron-ore deposits have been mined, while also allowing down-stream processes to be tailored to meet local requirements.

It also means Corus is a good fit. The industrial logic converged with a cultural affinity between the two groups' top executives early this year, reflecting the easy relations that usually exist between Indian and British firms. Tata Tea successfully took over Britain's Tetley Tea in 2000, linking Indian tea output to drinkers overseas, and this year Tata Consultancy Services (TCS), the group's software and services arm, set up a business-process outsourcing operation in Britain with Pearl, a life-assurance group. Both Corus and Tata executives talk about their desire for a friendly takeover and their common line on governance practices and business ethics. Tata also says that, in line with its record at NatSteel and Millennium Steel, it has no plans to close Corus plants or lay workers off—a bonus for Corus that might make it difficult for any rival bidder to succeed. (CSN, a Brazilian firm, is thought to be considering making its own bid for Corus.)

Mr Tata would become the chairman of the combined group with Jim Leng as deputy chairman, but he intends to leave the running of Corus to its existing executives, in conjunction with an integration committee that he will head. The deal would also restore the Tata Group to its traditional place as India's biggest conglomerate by revenues, ousting the more abrasive Reliance Industries from the top spot—a side-effect that Mr Tata and his colleagues are no doubt quietly relishing.

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Corporate crime

Jail time for Jeffrey

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Is the sentence handed to Enron's ex-boss excessive?

CONTRARY to expectations, Jeffrey Skilling did not receive America's longest-ever jail term for a white-collar crime this week. The sentence of 24 years and four months handed to the former boss of Enron on October 23rd is slightly less than the record-breaking 25 years in prison being served by Bernie Ebbers, the former boss of WorldCom.

Judge Sim Lake opted to set Mr Skilling's term at the low end of the range suggested by America's federal sentencing guidelines, which take into account the financial losses caused by the crime. In Mr Skilling's case, that meant up to 30 years and five months inside. The guidelines are no longer mandatory, so Mr Skilling's lawyers had sought a sentence of just seven to ten years, citing his good works in the community and the fact that his convictions for fraud and insider trading, connected with the collapse of Enron in 2001, were his first.

Not that Mr Skilling accepts the guilty verdict reached by the jury in May, when he was tried alongside Kenneth Lay, another former Enron boss who has since died. He says he is “innocent of all the charges” and plans to appeal. Among his complaints: holding the trial in Enron's home town, Houston, meant the jury was biased against him; prosecutors used threats of prosecution as co-conspirators to scare potentially sympathetic witnesses from testifying in his favour; and the judge misdirected the jury. Even so, the 52-year-old Mr Skilling may still be in jail when he is 70, given that there is no parole in federal sentences. His best hope is a 15% reduction in jail time for good behaviour.

Prosecutors and the public seemed delighted by Mr Skilling's long sentence. Yet there are growing worries about the severity of America's white-collar sentences, which treat bosses more harshly than drug dealers and some murderers. Twenty years ago, Mr Skilling would have got just seven years. America also treats white-collar offenders more severely than other rich countries. Nick Leeson, the “rogue trader” who brought down Barings Bank, served just four years of a six-and-a-half-year sentence. And South Korea's courts sentenced Kim Woo Choong, a former boss of Daewoo, to ten years—despite his fleeing the country after the group collapsed.

That Mr Skilling's sentence was so much harsher than that of Andrew Fastow, the former chief financial officer whose role in Enron's collapse was far clearer, has also caused disquiet. Lawyers feel that Mr Fastow, who received a six-year sentence last month, was rewarded for co-operating with prosecutors, while Mr Skilling was punished simply for asserting his constitutional right to go to trial.

His conviction and lengthy sentence highlight America's growing “criminalisation of agency costs”, says Larry Ribstein, a law professor at the University of Illinois. To get the benefits of diversified public ownership of firms, shareholders must delegate responsibility to managers, or agents. But agents do not always do the right thing by shareholders. Should such agency costs be handled by means other than criminal prosecutions and jail terms? Mr Ribstein thinks so. Civil litigation against managers and stricter corporate governance might be less costly and less likely to discourage legitimate risk-taking, he says. And Ellen Podgor of Stetson University College of Law in Florida questions whether long sentences have the deterrent effect that prosecutors claim, since “many who engaged in the conduct just did not see themselves as committing crimes.”

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Diesel in America

Second coming

Oct 26th 2006 | DETROIT
From The Economist print edition

Diesel is a dirty word to American motorists. But that could soon change

AFTER five years of delays American refiners are finally pumping new ultra-low-sulphur diesel fuel to service stations, to meet new regulations that took effect this month. Hitherto diesel contained up to 500 parts per million (ppm) of sulphur, but the new rules limit sulphur to 15 ppm. Will this new, cleaner diesel win over American motorists?

In Europe 50% of new cars run on diesel, rising to 70% in the premium segment, where diesel gets a tax break. In America the figure is just 3.6%. Detroit's Big Three manufacturers use diesel engines only in light trucks, such as the big Dodge Ram pickup. In contrast, European carmakers such as Mercedes-Benz and Volkswagen are growing more aggressive: VW offers American buyers diesel engines in several models, such as its Passat saloon and Touareg SUV.

Even so, diesel still has a bad name in America following Detroit's efforts to push rough, filthy and unreliable diesel engines in the 1970s and 1980s. Today's diesels are sturdy, smooth and up to 40% more fuel-efficient than petrol engines. They are also fast: an Audi diesel won the Le Mans 24-hour race this year. But the new cleaner fuel has come on stream just as regulators are clamping down on emissions of smog-causing nitrous oxides and soot-like particulates, which have been linked to lung cancer. Most carmakers are not ready with diesel engines that meet the new standards.

As a result Mercedes is temporarily limiting the availability of its E-class diesel, launched this month, to 45 states because it cannot yet meet the tougher standards imposed by California and some East Coast states. But Mercedes and VW are betting that from 2008 they will be able to meet the new standards with technology, such as the Benz Bluetec diesel, which adds ammonia to the exhaust gases to break down pollutants. This will make it possible to add diesel to a whole range of Mercs. Tom LaSorda, boss of DaimlerChrysler's American arm, expects to use Bluetec in a variety of Chryslers. Even long-sceptical Japanese firms such as Honda and Nissan are coming round to diesel.

Not everyone is so optimistic. General Motors is considering a diesel for some of its thirstiest trucks, such as the newly-redesigned Chevrolet Silverado pickup, but the firm's vice-chairman, Bob Lutz, frets that the extra cost of future pollution-control technology may price diesels out of the market.

So do not expect conversion on a European scale. J.D. Power and Associates, a market-research firm, forecasts that diesels will power just over 10% of American cars sold by 2015, or around twice the number of petrol-electric hybrids by that time. But at least both are greener than petrol-based cars.

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Lego's turnaround

Picking up the pieces

Oct 26th 2006 | BILLUND
From The Economist print edition

The venerable toymaker has recovered after a mistaken over-diversification

These are the toys you're looking for

“PLAY is nutrition for the soul,” begins Lego's description of itself, before going on to explain the Danish firm's philosophy of learning and development through play. For seven decades Europe's biggest toymaker—its name derived from *leg godt*, Danish for “play well”—has prospered with its ethereal corporate philosophy and openly professed disregard for maximising profits. Lego became a national treasure and one of the strongest brands in the toy industry. Its colourful bricks are sold in over 130 countries: everyone on earth has, on average, 52 of them.

Yet a couple of years ago the company's very survival was at risk. After six years of slowing sales and falling profits, Lego's crisis peaked in 2003, when it made a whopping DKr1.6 billion ($240m) operating loss on sales of DKr6.8 billion and was sitting on some DKr5 billion in debts. Rumours abounded that America's Mattel, the biggest toymaker, would take over its long-coveted European rival. Private-equity companies circled what they considered a perfect prey: a mismanaged, medium-sized firm in the hands of a single owner, the family of Ole Kirk Christiansen, a carpenter who founded the company in 1932.

Mr Christiansen's heirs decided to stand by the family business. They injected some DKr800m of their own money and appointed Jorgen Vig Knudstorp, a former management consultant at McKinsey, to get the company back on track. After speaking to toy retailers, who told him not to mess with Lego's brand or its core products, he decided to fix rather than reinvent the firm, which had gone astray when it branched out into businesses it did not understand.

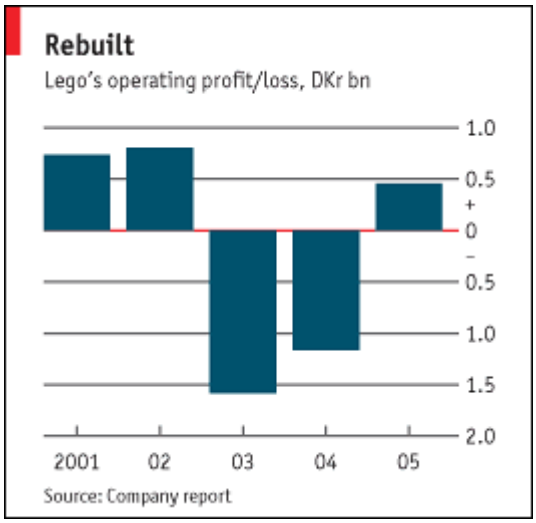
The logic of diversification was compelling, says Mr Knudstorp, but Lego went about it the wrong way. It tried to become a lifestyle brand with its own lines of clothes, watches and video games. And as it tried to attract more girls, it started to neglect its main customers, boys aged five to nine. “We had become arrogant—we didn't listen to customers any more,” says Mr Knudstorp. Lego was also hit by the general malaise in the traditional toy industry, which has been shrinking as a result of low-cost copycats, competition from high-tech gadgets, and falling birth rates in many developed countries.

Lego's turnaround plan, launched in March 2004, was painful. Around 3,500 of the firm's 8,000 employees were laid off, with more cuts to come: almost half the 2,400 workers in the firm's hometown of Billund will lose their jobs over the next three years. Factories in Switzerland and America are being closed down and production moved to Eastern Europe and Mexico. A majority stake in Lego's four

Legoland theme parks was sold to the Blackstone Group, a private-equity firm, last year. Assets in America, South Korea and Australia were sold off. The new boss also simplified the management structure and tried to foster a more commercial culture through a performance-based pay scheme and frank communication between management and employees. “We were not used to speaking about money,” says a Lego employee.

The Knudstorp cure is working. In August Lego reported pre-tax profits of DKr238m for the first half of 2006, compared with a loss of DKr202m for the same period last year. Sales were up by 19%.

Despite the greater focus on Lego's core business, some bits of the diversification strategy remain. Lego has continued to expand its Bionicle range and to launch new toys based on film tie-ins, notes Zsuzsanna Kantor of Euromonitor, a market-research firm. The Bionicle characters, futuristic figures based on elements of Polynesian mythology, were the first story-based franchise to be developed in-house, and have spawned books, cartoons and videos. Toys linked to the “Star Wars” and “Harry Potter” films continue to do well. And the latest “Lego Star Wars” video game (pictured), in which Lego figures re-enact the “Star Wars” saga, was a bestseller.



As Lego gets ready for the busiest shopping time of the year, the mood at the firm is festive. The toy industry has been stagnant for five years, says Gerrick Johnson, an analyst at BMO Capital Markets, but things are looking up. Mattel, Hasbro and other toymakers have reported strong results in the past couple of weeks. And with Lego preparing to celebrate its 75th birthday next year, Mr Knudstorp sounds confident when he says the firm can remain independent for another 75 years.

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Face value

Homo SAPiens

Oct 26th 2006
From The Economist print edition

Henning Kagermann defends his steering of Germany's business-software juggernaut

Landov

TAUNTS from Larry Ellison of Oracle, a big Silicon Valley software firm, cut no ice with Henning Kagermann, the boss of SAP, a rival software giant based in Walldorf, Germany. Last month Mr Ellison made wild claims that his firm had outperformed SAP tenfold and had established a two-year lead because of SAP's delays. He also claimed that SAP was abandoning its strategy of organic growth. Mr Kagermann did not respond personally, as Mr Ellison would no doubt have wished. Instead, his firm issued a statement denouncing Oracle's "complete misrepresentation" of the facts, and left analysts at Citigroup and Dresdner Kleinwort to pour scorn on Oracle's claims. Last week, when SAP reported solid results after a wobble in the previous quarter, Mr Kagermann insisted that SAP's performance "disproves our major competitor's claim", without naming names.

SAP and Oracle might appear outwardly similar, since both firms sell the software used by large companies to run their businesses, from inventory and resource planning to customer-relationship management. But they are very different. SAP, the industry leader, has grown organically, making only small acquisitions here and there to fill gaps. Oracle, in contrast, has grown rapidly in recent years as the result of a $19.5 billion acquisition spree, but is still far behind. And while the swashbuckling Mr Ellison is one of the software world's more colourful characters who enjoys taking potshots at his rivals, Mr Kagermann, a former physics professor, takes a more measured approach. His predecessor, Hasso Plattner, now SAP's chairman, was more in the Ellison mould, and clashes between the two men got personal. But a former colleague says Mr Kagermann prefers to see management as "dealing in shades of grey".

Mr Kagermann insists that SAP will not deviate from its organic-growth strategy, despite catcalls from Mr Ellison and some analysts' suggestions that it will not be able to maintain its double-digit growth in a consolidating industry without big acquisitions. SAP was founded by Mr Plattner and four other IBM dissidents in 1972, and its success stemmed from the quality of their programming, a masterpiece of German engineering. But buying other firms to gain access to their customers and increase market share, as Oracle does, is horribly messy from an engineering point of view, since it means maintaining several different products in parallel. SAP prefers to build everything itself.

Although SAP is now a global company, with research labs in India, China and California, its roots still unmistakably lie in Germany. That was brought home recently when three German employees were able to force the introduction of a workers' council—though 92% of the workforce voted against it—because of a quirk in German labour law. Some 60% of research and development is still done on the campus at

Walldorf, near Heidelberg, or at nearby universities; 90% of the staff in Germany are German. Some say that Shai Agassi, a charismatic young Israeli who is in charge of SAP's product development and is seen as Mr Kagermann's successor, is trying to draw the cutting-edge stuff to his base in California. Mr Agassi is a protégé of Mr Plattner and relishes SAP's rivalry with Oracle. So far Mr Kagermann has managed to keep his ambitious young lieutenant in check.

SAP is motoring along nicely under Mr Kagermann, but must avoid three obstacles if it is to maintain its leadership. The first is to keep its customers happy while encouraging them to upgrade to the latest versions of its products. This is tricky, since SAP's software is not renowned for its ease of use, and having trained their workers to use it, firms are often reluctant to change anything. “It's a resource-intensive system,” says one customer. “People need to apply themselves and follow the rules.” An SAP user group in Leipzig recently complained about the constant pressure to upgrade from SAP's venerable R/2 and R/3 software to its newer, more versatile mySAP and NetWeaver products. But Mr Kagermann insists that the upgrade is worthwhile, since the result is a flexible architecture that can be more quickly and easily customised, and more easily linked to other firms' systems.

The second challenge is to expand into the mid-market with products aimed at smaller firms, since most big ones already use SAP's software. By moving downstream, SAP hopes to expand its customer-base from 35,000 companies today to 100,000 by 2010, and double its addressable market to $70 billion. But selling software to small firms is difficult, so SAP relies on partners—including IBM, Microsoft and Accenture, plus thousands of smaller specialists—to sell and tailor its products. SAP's first customer was ICI, a chemicals giant; Mr Kagermann recently received an e-mail from one of its newest customers, a small winery in Baden-Württemberg, which has just purchased a system to track its operations from grape to bottle. The software was installed by a local partner in 15 days for €40,000.

At your service

The final test is to respond to the rise of “software as a service”—the delivery of software “on demand” via the internet, so that it runs inside a web browser. The best-known advocate of this approach, Marc Benioff of Salesforce.com, says it is far quicker and cheaper and signals “the end of software”. Mr Kagermann, needless to say, does not see things in such black-and-white terms. In future, he concedes, some software will be delivered in this way, but not all of it. SAP launched its first on-demand products this year, with more to come, particularly for smaller firms. But Mr Kagermann questions whether on-demand software is as customisable or as reliable as the traditional kind. SAP has pioneered a hybrid model, where software is delivered on-demand, but from a server on the customer's local network, thus providing the benefits of on-demand but without many of the drawbacks. It is just another example of how Mr Kagermann likes to see things in shades of grey.

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The American economy

Slow road ahead

Oct 26th 2006 | WASHINGTON, DC
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America's long-term potential rate of growth is falling, perhaps to its lowest pace in over a century

Get article background

EVERYONE knows that America's economy is slowing. Thanks to the bursting of the housing bubble, overall GDP growth has fallen back sharply. The biggest short-term uncertainty for the world economy is whether American consumers stop spending and drag the country into recession. But beyond the business cycle, another slowdown has received scant attention. America's potential rate of growth—that is, the pace at which annual output can expand without pushing up inflation—is also falling. By some estimates, it could drop to 2.5% over the next few years, which would be the slowest pace in over a century.

If that happens, the consequences will be serious. Tax revenues will grow more slowly than expected. Monetary policy will become harder to manage: as the 1970s showed, inflation can get out of control if central bankers do not realise that an economy's speed limit has fallen. Financial markets will be disturbed as conventional wisdom adjusts from an assumption of 3-3.5% potential output growth, and investors downgrade their expectations.

Potential output is hard to estimate, let alone predict. That is because an economy's trend growth rate cannot be measured directly. It has to be inferred. Over the long run economic growth depends on two things: increases in the supply and productivity of labour. The growth of labour supply, in turn, depends on the growth of the working-age population, the proportion of people who work and the number of hours they put in. The pace of productivity growth depends on capital investment, improvements in business processes and technological innovation. By looking at such trends, economists can estimate future potential output.

Although it generates precise-looking forecasts, this kind of “growth accounting” is fraught with difficulty. Both labour supply and productivity growth bounce around during business cycles. The share of people

willing to work may fall in a recession, for instance, as discouraged people temporarily drop out of the workforce. Once job prospects pick up, they might return. Productivity growth is usually higher at the beginning of an expansion than at its end as firms work their existing employees harder before hiring new people. As a result, potential output can temporarily diverge from its underlying trends, making it even harder to estimate.

Nonetheless, the broad post-war history of America's underlying growth rate is clear. In the 1960s potential output accelerated to around 4% a year, largely because more women got jobs. In the early 1970s, for reasons that are still ill-understood, productivity growth slowed sharply, pulling down the trend rate of growth. Between the mid-1970s and mid-1990s America's economic speed limit was about 3%. Around half that growth came from an expanding workforce; the other half from productivity growth.

Thanks mainly to higher productivity growth, but also to a rise in the number of Americans working, trend growth rose suddenly in the mid-1990s. After the 2001 recession, productivity growth accelerated again, while the growth of labour supply slowed sharply. The share of working-age Americans in jobs fell after rising almost continuously for over four decades (see chart 1). This fall was widely interpreted as temporary, a sign that the recession was deeper than it appeared. But after five years of expansion, it has not been reversed, suggesting (although the evidence is still tentative) that structural changes are afoot. These labour-markets shifts are the main reason to be pessimistic about America's potential output growth.

So why is the proportion of Americans who work falling? For three reasons. First, the baby-boomers are heading towards retirement. The share of people aged between 55 and 64 has risen from 10.5% in 1995 to 13.3% in 2005 and is likely to reach over 16% by 2015. People over 55 tend to work much less than younger folk.

Second, the rush of women into the workplace has stopped. The proportion of women working rose from below 40% in 1960 to a peak of over 60% in 1999. It has subsequently fallen slightly.

Third, the rate of teenage employment has plunged. In the 1990s over 50% of young people aged 16-19 had jobs. Today just over 40% do, the biggest drop since records began. This decline is a bit of a mystery, since job growth in the kinds of industries that tend to employ young people—restaurants and shops—has been well above the national average. It may have happened because teenagers are staying at school or college longer, and are working less on the side. More education may mean higher future productivity, but in the medium term it cuts the number of available workers.

If economists at the Federal Reserve in Washington, DC, are right, these three components are likely to result in a bigger change than has hitherto been expected. A recent study* suggests that America's trend rate of labour-force participation could drop by a further 1.4 percentage points in the next four years, to just over 64%. By combining these projections with the Census Bureau's estimates for the growth in the working-age population, they calculate likely changes in the overall supply of workers. By 2010, the Fed economists reckon, labour supply in America will be rising by a mere 0.4% a year, well under half its current rate.

The geezer difference

These projections could be too gloomy. Washington's official number-crunchers, such as the Congressional Budget Office, predict that labour-force growth will slow down, but not that dramatically. An unexpected jump in what Dick Berner of Morgan Stanley calls the “geezer labour force” could make a difference as ageing baby-boomers work longer. Men in their 60s are already the fastest-growing segment of the workforce, although this has not made up for the overall decline.

A rise in immigration could increase the supply of labour, too, particularly since the proportion of immigrants who work is higher than that of native-born Americans. As the labour shortage begins to bite, the demand for immigrants should rise. But the politics of the issue argue against a big rise in the next few years. The government is under increasing pressure to crack down on employers who hire illegal

workers, and Congress recently passed legislation to build a fence along a large stretch of the Mexican border.

It seems very likely, then, that America's labour supply will grow more slowly. And if that happens, potential output growth will too, unless productivity growth accelerates.

Unfortunately, the latest evidence suggests that, if anything, productivity growth is slowing unexpectedly. Over the past two years, in the non-farm business sector, it slowed to an annual average of 2% from an average of almost 4% in the previous three years.

And even that figure may be too high. The Bureau of Labour Statistics recently said 810,000 more jobs were created between March 2005 and March 2006 than they first thought. Thanks to those extra jobs the productivity figures for 2005 may be revised down by a further half of a percentage point. For the economy as a whole, the figure is some 0.3-0.5 percentage points lower than the official productivity figures suggest, because productivity growth in farming and government, which are left out of those figures, is even lower.

The longer the economy's expansion goes on, the slower productivity growth is bound to be. But the pace of the deceleration has begun to raise concerns. The small band of economists who study these things now agree that underlying productivity growth rose sharply in the late 1990s, from around 1.5% to some 2.8%. Three of those experts, Dale Jorgenson, of Harvard University, Kevin Stiroh, of the New York Fed and Mun Ho, also of Harvard, have calculated that over 60% of the late 1990s productivity surge was related to information technology. The industries that saw the biggest productivity gains were those that used IT most intensively.

The 2001-04 productivity surge is now the focus of an argument with big implications. Only 30% of that acceleration was related to IT, says Mr Jorgenson and his colleagues. Optimists take that as a good sign. It shows improvements in business processes spawned by the IT revolution are spreading through the broader economy. The economists reckon underlying business productivity growth is now around 2.5% (or around 2.2% in the overall economy). This is slower than in the late 1990s, but still far above historical averages.

Others are more worried. Robert Gordon, of Northwestern University, reckons that the post-2001 acceleration was the result of cost-cutting, not innovation. Other economists note that the pace of investment, particularly in IT, is much lower than it was in the 1990s. JPMorgan's calculations, for instance, show that firms' spending on IT equipment has grown by only 5.5% a year in this expansionary period, compared with over 20% a year in the late 1990s. Lower capital spending, they fear, could be a harbinger of slower productivity growth. Morgan Stanley's Mr Berner worries that high oil prices may also have hurt underlying productivity growth, by shifting the relative profitability of different sectors of the economy (much as the oil shocks of the 1970s did).

Mr Gordon sees the underlying rate of business productivity growth slowing to below 2.5% which, by his calculations, implies a rate of 2.1% for the overall economy. Coupled with the slowdown in labour supply, he concludes that America's potential growth rate could fall to 2.5%. Although their predictions for productivity and labour supply are different, JPMorgan's economists agree with his figure.

Mr Gordon's calculations suggest that 2.5% would be America's slowest economic speed limit in over a century (see chart 2). That is less surprising than it sounds. Though the statistics are less reliable for the years before 1950, it seems that in the early 20th century potential output grew rapidly thanks both to technological innovation and rapid immigration. Although actual output tumbled during the 1930s, America's potential growth rate did not. Some scholars argue that the 1930s were among the most technologically innovative years of the century.

Since no one foresaw the productivity revolution of the mid-1990s, these predictions could prove too pessimistic. The next “killer application” could be just around the corner. Even without rapid investment, the IT revolution may yield more productivity gains. But without some such happy chance, it looks as though America's potential growth rate is heading for a slowdown, at least for the next few years. The

sooner that investors and policymakers wake up to this, the smoother the adjustment is likely to be.

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* "The recent decline in the labour force participation rate and its implications for potential labour supply", by Stephanie Aaronson, Bruce Fallick, Andrew Figura, Jonathan Pingle and William Wascher. *Brookings Papers on Economic Activity*, 2006:1

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Consumer banking

A broad, thin umbrella

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Landov

Is Citigroup, the world's biggest bank, big enough where it matters?

AFTER the string of scandals that has rocked Citigroup, the world's biggest bank, in recent years, one might think it would open its trademark umbrella and take cover. Instead, Chuck Prince, Citi's chief executive, has been out and about. On October 27th, just a week after Citi announced disappointing third-quarter profits, Mr Prince and his crew are hosting another conference call to tell investors how its heavy investment spending is panning out. In doing so, he hopes to convince Citi's many critics that it is now opening its stride, not hunching its shoulders.

A bank of Citi's heft and complexity cannot change overnight, Mr Prince says, with reason. His predecessor, Sandy Weill, built a financial-services juggernaut by snapping up companies on the cheap, wringing out the costs, then buying more. But he put little thought into how the pieces could fit together, nor how his sprawling machine could be steered.

On taking over, Mr Prince's first job was to get the regulator off Citi's back; his second, to rediscover an engine of growth under all of Mr Weill's bolted-on body-parts. His answer was to do some things his predecessor had neglected, and to undo other things Mr Weill should have left alone. He sold various insurance businesses that did not fit his vision. He also began investing in the areas that Mr Weill, in his zest for cutting costs, ignored: bank branches, internal controls, product development and technology to weld together Citi's many parts.

So can an unencumbered Citibank grow? The answer depends heavily on Citi's consumer business—corporate banking accounts for only a third of its profits, retail most of the rest—and also, it says, on opportunities abroad. Citi, like its rivals, hopes to cash in on two big trends: the growing middle class in emerging markets, which will need to borrow money for cars, homes and university tuition; and the growing numbers of multinational companies that require bankers who can do business from Kazakhstan to Canada.

Citigroup, with offices in over 100 countries and 80m customer accounts outside its home country, is by far the most cosmopolitan American bank. Last year it pocketed $2.7 billion in profits from its international consumer business. It has opened 574 bank and consumer-finance branches so far this year, mostly in faster-growing places like India. Earlier this month it bought a fifth of Akbank, a Turkish

bank, and it is said to be in the running for China's Guangdong Development Bank. Only HSBC, a British bank, and GE Capital come close to matching its breadth of reach and depth of local knowledge.

But this globetrotting has so far yielded meagre returns. Revenues from Citi's international consumer business were flat in the third quarter, compared with the second. The danger, says David Hendler of CreditSights, is that Citi spreads itself too thinly. Despite its vast size overall, it may not grow big enough in any market to be really profitable. With the exception of Mexico, where it bought Banamex, one of the country's largest banks, Citi still lacks a commanding presence in most attractive international markets. It thus fails to benefit from economies of scale in marketing, technology and the collection of credit-history data, which is vital where formal credit bureaus do not exist. Nor can its modest retail banks attract much custom for the other businesses, such as stockbroking, under the Citibank umbrella.

Optimists say Citi's small size in these markets gives it more room to grow, especially as its main competitors are relatively unsophisticated local banks. But the locals have other things going for them. Regulation is one. India, for instance, does not allow foreign banks to wholly own domestic ones. Citi has dodged this rule by opening “consumer-finance branches”, which lend but do not collect deposits. But it now has only 409, compared with the thousands of branches of its local rivals. In other countries, like Turkey or Brazil, there are few, if any, opportunities to buy a bank outright. This leaves Citi with no choice but to take small stakes in local banks or build branches from scratch—a painstaking process.

For all of Citi's vaunted internationalism, it still makes 57% of its profits at home. Unfortunately, it faces similar problems there. It is America's sixth-biggest bank in deposits, with a 3.5% share, according to SNL Financial, a research firm. Bank of America (BoA), the country's largest and most profitable retail bank, is almost three times bigger. At home, as abroad, Citi is spread widely, but finely. According to Dominion Bond Rating Service, it holds less than a tenth of the branch market-share, in every state. It thus loses out to the likes of Wachovia and BoA, which dominate their favoured markets and enjoy operational efficiencies as a result.

For example, Citi's competitors can dip into a deep well of cheap deposits to finance their loans. Citi, by contrast, must raise money on the markets. It has thus suffered more than its peers from rising borrowing costs. To attract more deposits, Citi is offering generous interest rates to new customers of its online bank. It is also launching its first branches in places like Boston, on the untested theory that it can convince its brokerage and credit-card customers there to bank with it too.

Mr Prince is counting on such investments to help Citi grow organically. But investors are impatient. So are some of Citi's investment bankers. Despite losses in fixed-income trading in the third quarter, Citi's investment bank does quite well—its proud money-movers see themselves as peers of Goldman Sachs. But despite their relative success they have watched Citi's stock price flounder since 2001, dragged down by its flailing retail side. Worse still, they have recently seen their salaries squeezed in the name of controlling costs. Investment bankers—like Citi's investors—may wonder how long they have to suffer for the travails of Citi's consumer business. Golden parachutes, not red umbrellas, may be on their minds.

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Buttonwood

Send in the clones

Oct 26th 2006
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A cheap alternative to hedge funds

HEDGE funds profit handsomely from their mystique. The typical client imagines they generate lots of money, doesn't know quite how they do it, and is willing to pay their high fees as a result. But some academics now think it is possible to make cheap, knock-off versions of these expensive originals. Perhaps you can get Saks Fifth Avenue products at street-market prices.

Such a product would certainly be popular. Many investors would like to hedge their portfolios. They may have bet too much money on shares, but feel that buying bonds would lock them into low returns. Hedge funds seem to offer share-like returns with much lower volatility.

The problem is the cost. Funds routinely charge 2% a year on the money invested and claim a fifth of all profits. Often investors also have to pay a second layer of fees to fund-of-funds managers, who spread their clients' money across the vast hedge-fund universe.

But financial scholars are beginning to demystify hedge funds. They think they can replicate their performance using garden-variety financial products. The result could be a cheap competitor for the hedge-fund titans, akin to the index-tracking funds that have eaten into the market shares of active fund managers.

Replication is possible because hedge-fund managers are not as distinctive as they claim. They say their returns are based on skill, or “alpha”, but in fact their performance is largely derived from market movements. A recent paper* by two academics at the Massachusetts Institute of Technology breaks down the returns of 1,610 funds from 1986 to 2005. It finds that six common factors, such as the change in the S&P 500 index and the return on corporate bonds, explained a significant part of hedge-fund returns.

Investors can gain exposure to these factors through widely available liquid instruments. Thus it should be possible to build “clone” portfolios that resemble hedge funds. Such portfolios would not only avoid hedge-fund fees, but would also escape the risk of backing a mismanaged fund, such as Amaranth, which lost 65% of its value in September.

The authors suggest cloning a fund by dissecting its performance over the past year or two. One could sift and sort the factors behind its success, and allocate the clone's money accordingly. A back-tested clone portfolio returned an average of 12.8% a year over nearly 20 years compared with 14.2% for the typical hedge fund. And the copycat portfolio offered investors many of the same benefits of diversification as the fund it mimicked.

Not every academic is impressed by this approach, however. Harry Kat, at the Cass Business School, says that such “multi-factor” models fail to explain a large proportion of hedge-fund returns. But Mr Kat proposes his own cheap alternative†. It may be impossible to know the particular plays hedge-fund managers make. But, he says, you can devise a formulaic trading strategy in the futures markets that would duplicate the overall shape of their returns. His strategies would give investors two of the three things they look for from a hedge: a low correlation with their existing portfolio, at a level of volatility they can tolerate. The return would be out of their hands, but tests suggest profits can be decent: 10% a year in one example.

Alternatively, Benjamin Bowler of Merrill Lynch suggests investing in hedge-fund niches, such as merger arbitrage. Instead of spending time and money investigating which takeovers to back, a mechanical strategy could back all deals that met certain parameters. This, too, could be done at low cost.

Will such strategies be introduced in practice? Clones may be cheap to run, but you would need a big chunk of capital to set one up. Unfortunately, the financial institutions that have the money are quite happy with the status quo, which is highly profitable for both hedge-fund managers and the investment banks that service them. This golden goose is a highly protected species.

But the mystique enjoyed by hedge-fund managers may not last for ever. Another study††, examining the performance of funds-of-funds from 1995 to 2004, found that their performance depended rather little on managerial skill, except during the dotcom bubble. Furthermore, those few managers who did distinguish themselves were then inundated with more money than they could handle. Often, the search for a skilful manager turns out to be a wild-golden-goose chase.

Investors may be suspicious of cheap reproductions. But originality comes at a price. Those who cannot afford the boutiques may one day throng to the knock-off merchants.

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* "Can Hedge Fund Returns Be Replicated? The Linear Case", by Jasmina Hasanhodzic and Andrew Lo

† "Tell Me What You Want, What You Really, Really Want!", by Harry Kat and Helder Palaro

†† "Hedge Funds: Performance, Risk and Capital Formation", by William Fung, David Hsieh, Narayan Naik and Tarun Ramadorai

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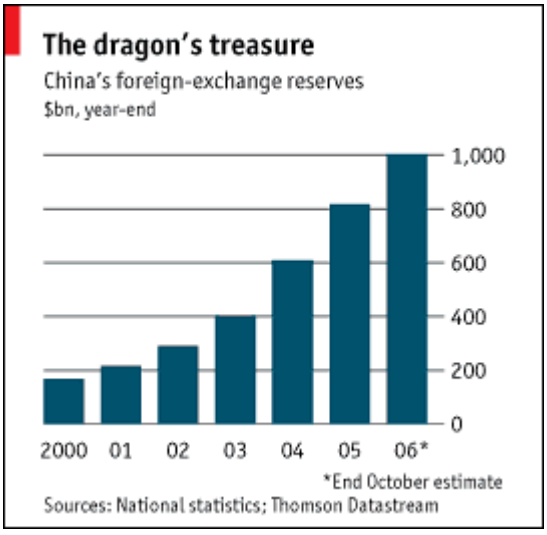
About sponsorship

China's foreign reserves

Who wants to be a trillionaire?

Oct 26th 2006 | HONG KONG
From The Economist print edition

Not China's central bank



BY THE end of October China's foreign-exchange reserves are likely to top $1 trillion, twice their level two years ago and more than one-fifth of global reserves. This handsome sum would be enough to buy all the gold sitting in central banks' vaults (indeed, twice over) or almost all of London's residential property.

China's massive hoard is the result of its large current-account surplus, significant inward foreign direct investment, and big inflows of speculative capital over the past couple of years. In theory, flows of foreign money into China should push up the yuan, but China has resisted this, forcing the central bank to buy up the surplus foreign currency. The growth in reserves has slowed in recent months, but it is still averaging a hefty $16 billion a month.

China's official reserves already far exceed what is required to ensure financial stability. As a rule of thumb, a country needs enough foreign exchange to cover three months' imports or to settle its short-term foreign debt. China's reserves are equivalent to 15 months of imports and are six times bigger than its short-term debt. The explosion in reserves is also a headache for the central bank. It creates excess liquidity, which risks fuelling higher inflation, asset-price bubbles and imprudent bank lending.

There are two simple ways to stop reserves rising. China could set free its exchange rate or it could relax restrictions on capital outflows and allow private citizens to hold foreign assets. Significant moves of either kind seem unlikely in the near future. So long as China runs a large external surplus (the natural result of its high saving rate) and refuses to set its currency free, its stash of foreign currency will probably continue to mount.

How that money is invested has big implications for the world economy, not just for China. Brad Setser, head of global research at Roubini Global Economics, estimates that about 70% of it is invested in dollars, mainly Treasury securities. This has propped up the dollar and reduced American bond yields—by up to 1.5 percentage points according to some estimates. A big shift out of dollars could therefore push up bond yields and hence mortgage rates, damaging America's already crumbling housing market.

China's central bank is thought to be switching from Treasury bonds to American mortgage-backed securities and corporate bonds in an attempt to earn higher yields. Chinese officials have also discussed in private the need to diversify reserves out of dollars in order to reduce exposure to a big drop in the greenback. The bank may be putting a bigger slice of any increase in reserves into euros and emerging Asian currencies, but so far there is little sign of a shift out of its existing stock of dollars. One problem is that China's investments are so big that they move markets. Shifting money into euros would push down the dollar. China would then not only suffer a capital loss on its remaining dollar reserves, but it could also be forced to buy yet more reserves to hold its currency down against a weaker dollar.

Fear of a capital loss, and dissatisfaction with unrewarding yields, have triggered a flurry of ideas on how to put the money to better use. One popular idea is to use some of China's reserves to buy oil and other commodities. The snag is that stockpiling oil would push up prices, yet absorb only a tiny proportion of the sums at China's disposal. Buying the equivalent of six-months' oil consumption, as has been

suggested, would take only 8% of total reserves at current prices, but the extra oil bought would amount to three times the growth in global oil demand this year. Buying gold would have similar results: if China invested just 5% of its reserves in gold, it could buy the world's entire annual mine production.

Another proposal is to spend more money on infrastructure investment, which would yield a much higher return than American bonds. However, since China's investment already accounts for 40% of GDP, it is not clear that China needs more. Writing off banks' non-performing loans might seem more sensible. In 2004 and 2005 the People's Bank of China did indeed shift $60 billion to state banks. The remaining stock of bad loans is now around $250 billion, according to UBS.

By buying American bonds, China is subsidising rich American consumers while China's health care, education and social safety net are starved of funds. So why not use reserves to relieve rural poverty, improve health care, or inject money into the under-funded pension system?

Unfortunately, all of these proposals to spend money at home misunderstand the nature of foreign reserves. The problem is that conversion of the foreign currency into yuan would put upward pressure on the yuan and so force the central bank to buy yet more foreign currency to hold it down. Reserves would return to their original level.

The only real solution to the poor return on China's reserves is to stop accumulating them. That requires policy reforms to reduce China's massive saving, which drives its current-account surplus, and a more flexible exchange-rate system. But before that happens, China's reserves could well hit $2 trillion.

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Hong Kong property

Peaks, valleys and harbours

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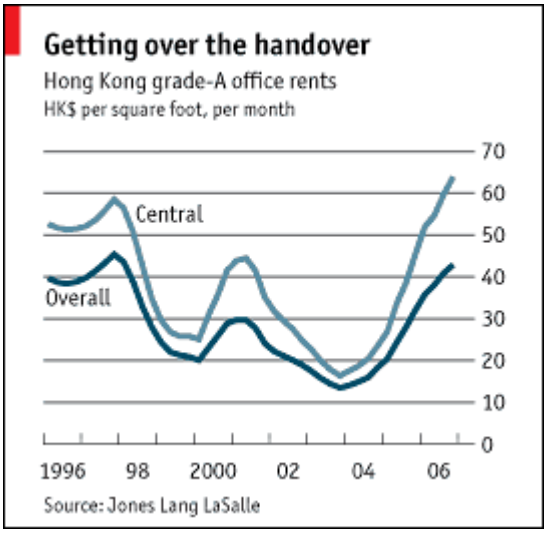
Hong Kong's rents are at their highest since the Brits left



PROPERTY prices have always served as a gauge of confidence in Hong Kong, a city known for its boom-and-bust cycles. There is more than passing interest, then, in the current scramble for classy properties in the central business district. Harbour views have attracted investment banks, hedge funds, private-equity firms, and executive recruiters, all desperately seeking an address meant to impress.

Real-estate prices in Central, as the area is called, are up by 290% on average since the third quarter of 2003, according to Jones Lang LaSalle, a consultancy. The increases at the top end of the market have been even higher. That makes central Hong Kong space 20% more expensive than equivalent space in Tokyo, Asia's second priciest market. Residential rents are soaring as well, with prices for nice flats of 1,700 square feet (158 square metres) or more rising by 15-25% over the summer.

Not long ago, the picture was very different. Back in 2003, the lingering impact of the Asian financial crises, the bursting of the dotcom bubble, and SARS resulted in a much gloomier economic picture. High-paying jobs disappeared; foreigners left; restaurants closed; rents plunged and landlords cut whatever deals they could.

With remarkable bad timing, a big and glamorous skyscraper was nearing completion at the time. Known as Two ifc, the building reached 88 storeys with almost 1m square feet of top-quality office space. The only thing it lacked was tenants. In something of a panic, a deal was cobbled together to entice UBS, an investment bank, to take 170,000 square feet at a rumoured price of HK$14 to HK$20 ($1.80 to $2.57) a square foot per month.

The UBS deal is now seen as an investment coup. In August this year, an unnamed tenant renewed its lease in the same building at HK$130 per square foot. With a vacancy rate close to zero, it is doubtful that many other firms will manage to squeeze their way in. If and when they do, rates will be higher still.

Eventually, today's high rents will lead to more supply in the market, but not soon. New construction in Central stalled after the slump several years ago. Now, with just a single new building due to come on to the downtown market in the near future—a relatively small, 14-floor tower of 115,000 square-feet—the leasing agent, Jones Lang LaSalle, has been deluged with calls. Legg Mason, an investment firm, has snared some space in the building, and a few other deals have been signed. But the landlord is in no great rush: prices, after all, are rising.

The same holds true in residential property. Many buildings have waiting lists. And, just as on the commercial side, the soft market of several years ago means there is little new construction under way.

But not every sort of property is seeing prices shoot up so fast. In real estate, the two contrasting sides of Hong Kong are starkly apparent: the one that is home to a global services sector is booming; the one that is home to a less glamorous manufacturing sector—much of it leaving for mainland China—is struggling. Outside of the financial district, prices on commercial property are still well below their highs.

Oddly, the construction now under way is mostly in the areas where demand is not particularly strong. These include the eastern end of Hong Kong Island and two new districts in the Kowloon peninsula, where the world's third-tallest building—due to be 118 storeys—has begun to rise. These developments are all a bit of a gamble: they may be high quality, but seem to fail the location test. To be fair, though, three years ago the same was being said about most of Hong Kong.

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Venezuela and Argentina

The Chávez play

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Venezuela's president tries his hand at financial arbitrage

Get article background

JUST as Venezuela is known for its exports of crude, Argentina is famous for its exports of IOUs. Less than two years after it handed its creditors a world-record loss in a sovereign debt-exchange, Argentina's government has found an eager new patron in its oil-rich ally. Over the last year, the government in Caracas has bought some $3.1 billion in Argentine bonds. Is this a case of Hugo Chávez, Venezuela's tub-thumping president, putting political solidarity ahead of fiscal prudence? Look closer.

Reuters

A slaphappy deal between Kirchner and Chávez

The roots of the deal lie in the currency controls Mr Chávez imposed on his country during the economic meltdown of 2003. To halt capital flight, he pegged the bolívar, Venezuela's currency, to the dollar (the official rate is now 2,150 to 1), and sharply curtailed opportunities to buy dollars at that price. As a result, a black market in foreign exchange soon opened up. The bolívar could not hold its value at the kerbside—a dollar has traded for anything from 2,400 to 2,900 bolívars in the past year—adding to inflationary pressures.

However, unlike most of his countrymen, Mr Chávez can help himself to dollars from the state oil company, PDVSA, or from his own central bank at the official rate. This he did to acquire the $3.1 billion he needed to buy the dollar bonds from Argentina's government, which started issuing debt with indecent haste after completing its huge bond restructuring in mid-2005. Argentina's president, Néstor Kirchner, was more than pleased to borrow directly from Venezuela. Doing business with a fellow Latin American leftist is more palatable than asking for money from the private international lenders he repeatedly bashes. Moreover, Mr Chávez was, in effect, offering to underwrite his debt issue. Venezuela's big purchases meant that Mr Kirchner did not need to test the market's appetite for his government's bonds too deeply.

But almost as soon as he got the Argentine paper, Mr Chávez began to sell it to local Venezuelan banks, at the rate of 2,400 bolívars to the dollar. All told, his government off-loaded $2.4 billion-worth of bonds, pocketing a tidy profit. How tidy? His finance team eagerly announced a gain of $309m to the press last month; though the true figure may be a bit different.

The banks too were happy. They were free to sell the bonds abroad for dollars, which they promptly did for a handsome profit. Some of them converted the greenbacks back into bolívars at black-market rates,

others hung on to them. Either way, this new source of foreign exchange has relieved pressure on the black market; the bolívar has stabilised and one source of inflationary pressure has eased.

Within Venezuela, critics have complained not about the deal itself, but about who was in on it, and who wasn't. The government has still not revealed its method of choosing which banks would be eligible for a chunk of the massive return Mr Chávez was offering. “Any operation that hands out $300m discretionally, regardless of the mechanism, is a clear incentive for corruption,” says Alejandro Grisanti of the Caracas consultancy Ecoanalítica. In the absence of an open bidding process, government officials were free to route the Argentine bonds to banks already supportive of Mr Chávez, to tie the sale to future support, or to receive payments or favours in exchange for offering them.

But despite this carping, can the two presidents not congratulate themselves on a clever financial manoeuvre that had something for everybody who was party to it? Argentina's government found a reliable customer for its debt; Mr Chávez achieved lower inflation and a $309m profit for the Venezuelan exchequer; and the local banks divvied up a further gain of $250m-300m.

Unfortunately, there are no free lunches, and there is one big, hidden loser in this transaction: the Venezuelan central bank. Mr Chávez, in effect, plundered its reserves for about $580m, both by forcing it to sell him dollars at the official exchange rate, and by taking dollars from the state oil company that traditionally went to the central bank. That is a heavy loss to the country, which might need its reserves in a pinch. “But no one's going to complain,” says Walter Molano of BCP Securities, “because nobody owns that money.”

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About sponsorship

Mobile telephony and banking

Phoney finance

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Most South Africans do not have bank accounts. But most do have mobile phones

LIFE is now easier for Andile Mbatha, who owns a hair salon in Soweto. Gone are his days of trekking to his bank, which could take two hours by minibus, to send money to relatives. Nor does he keep piles of cash in his salon any more. Last year, he opened a bank account with Wizzit, an innovative provider of financial services. He now sends money to his sister in Cape Town whenever he wants, from wherever he wants, using a simple menu on his mobile phone. Half his customers no longer pay cash for their haircuts. They use their phones to move money from their accounts to his, in a few seconds. “This has taken out a lot of stress,” says Mr Mbatha.

About half a million South Africans now use their mobile phones as a bank. Besides sending money to relatives and paying for goods, they can check balances, buy mobile airtime and settle utility bills. Traditional banks offer mobile banking as an added service to existing customers, most of whom are quite well off. But Wizzit, and to some extent First National Bank (FNB) and MTN Banking (a joint venture between Standard Bank and a mobile-phone network), are chasing another market: the 16m South Africans, over half of the adult population, with no bank account. Significantly, 30% of these people do have mobile phones. Wizzit hired and trained over 2,000 unemployed people, known as Wizzkids, to drum up business. It worked: eight out of ten Wizzit customers previously had no bank account and had never used an ATM.

Mobile banking is just one example of a wider phenomenon in South Africa. With its odd mix of advanced capitalism and developing-world economics, the country is successfully luring people who hitherto dealt only in cash or barter to the world of formal finance. A simplified kind of account called Mzansi was launched in 2004 to reach the unbanked, and portable banks and ATMs have been rolled out in townships and in the countryside. To this fast-changing scene, mobile-phone banking looks to be a promising addition. Millions of South Africans send money to their relatives in other parts of the country. And most of these sums, which add up to about 12 billion rand ($1.5 billion) each year, still move informally.

South Africa is not the first place to use mobile-phone banking: countries such as Japan, South Korea and the Philippines have had it for a while. But the potential is probably bigger in the developing world, and in countries in which migrants remit money to their families in relatively poor homelands. In Greece, a European Union member that is now awash with migrant labour, Albanians or Bulgarians often send money home by putting crumpled banknotes in the hands of a trusted compatriot, who takes a cut. If they could do it all by pressing buttons, they would.

In most of Africa, meanwhile, only a fraction of people have bank accounts—but there is huge demand for cheap and convenient ways to send money and buy prepaid services such as airtime. Many Africans, having skipped landlines and jumped to mobiles, already use prepaid airtime as a way of transferring money.

They could now leap from a world of cash to cellular banking. In Kenya, a pilot scheme called M-Pesa is being used to disburse and pay micro-loans by phone. Meanwhile Celpay, which FNB bought last year from Celtel, a mobile-phone company, is offering platforms for banks and phone companies in Zambia and Congo. In countries like Somalia, with chaotic conditions at home and a huge diaspora, cash transfers by phone would be a boon.

For banks, persuading people not to use branches for simple transactions such as balance enquiries or transfers should reduce operating costs. So far, they charge the same for mobile as for traditional banking, though Wizzit says its services are at least a third cheaper than those of a traditional bank.

But drawing the unbanked into the joys of cell-finance isn't always easy. Many think banking too expensive and complicated, and helping new customers become financially literate takes time. The technology remains clunky in some cases, with downloads requiring dozens of text messages. Several rival platforms are still in the fight, but so far those that emphasise simplicity and ease-of-use over state-of-the-art technology and security have made the greatest strides. A lot also hangs on putting in place the right laws and regulations. They need to be tight enough to protect vulnerable users and discourage money laundering, but open enough to allow innovative mobile banking to grow.

If the transfer of money by mobile phone—between countries as well as within them—takes off, it could have implications far beyond the salons of Soweto. In 2005, according to the United Nations, global migrants remitted $232 billion, of which up to 20% was lost on the way, mostly in bank charges or fraud. If cellular transfers could slash that figure, mobile banking would prove to be a good call.

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Economics focus

Hard currency, tight spot

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The euro is a cause of Italy's problems, but also a balm for them

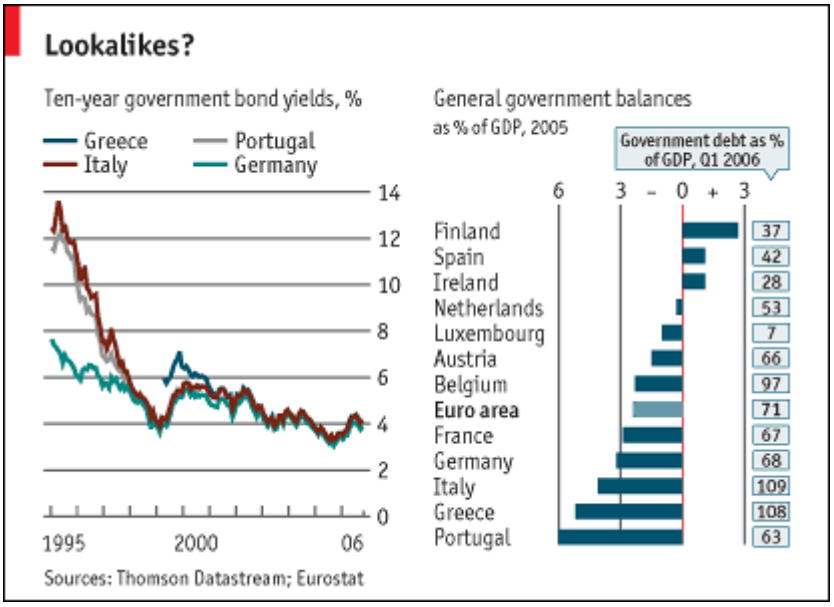
Illustrations

CHARGED with the thankless task of knocking Italy's public finances into shape, Tommaso Padoa-Schioppa is doing his best. Alas, two top rating agencies think his best won't do. The finance minister faces a big budget deficit (4.1% of GDP last year) and mountainous public debt (in gross terms, 109% of GDP). But Standard & Poor's and Fitch say Mr Padoa-Schioppa's recent budget does too little. They think it relies too much on raising taxes and not enough on cutting spending, which economists say is a surer path to lasting fiscal sobriety. They are less optimistic than the minister about how much a crackdown on tax evasion can bring in. And they detect accounting jiggery-pokery too. Last week the agencies downgraded Italy's sovereign debt.

Italy's public finances are not its only problem. Its recent growth rate has been pathetic—it may manage 1.5% this year, after four years below 1%—as its companies have struggled to keep pace with competitors elsewhere in the euro zone: unit labour costs, relative to Germany's, have risen by more than 20% since 2000. An obvious (if temporary) solution, devaluation, is not possible within a currency union. Though it may seem far-fetched, some people believe that Italy might be pushed out of the euro zone. In a recent pamphlet Simon Tilford, of the Centre for European Reform, a London think-tank, puts the probability as high as 40%.

You might conclude that a slow-growing, highly indebted country such as Italy finds the euro zone an uncomfortable place to be. Not at all. Precisely because it is a member of the single-currency club, Italy has, considering the state of its books and businesses, been remarkably well regarded by the bond markets. Its ten-year bonds yield a mere 4.15% or so, only about 30 basis points (0.3 percentage points) more than their German equivalents. The markets are just as kind to other euro-zone spendthrifts. Government bonds from Greece (deficit last year, 5.2% of GDP; debt, 108%; but GDP growth, healthy) yield about the same as Italy's. Those from Portugal (deficit, 6%; debt, 63%; growth, perkier this year after a feeble run) yield ten basis points less.

One reason why bond yields are low across the euro area is that inflation is under control and expected to stay that way. But the market's failure to discriminate among euro-member bonds is striking nonetheless. Part of the explanation is that yields in general, including those on emerging-market debt are low, leaving little room to separate borrowers. Another reason, however, is the creation of the euro itself. In the years leading up to the currency's birth, investors came to realise that the risk of devaluation was evaporating. As a result, the spread (or premium) they demand to compensate them for this risk tumbled (see left-hand chart). It also helps that the European Central Bank (ECB) accepts members' sovereign bonds as collateral on even terms—provided they retain a credit rating of A- or above. And though the ECB insists it will not rescue governments from the consequences of their fiscal folly, markets may believe otherwise, calculating that if a country looked like defaulting it would be bailed out somehow. The upshot is that now one government's debt looks much like any other's.



Cheaper borrowing gives governments little incentive to tighten their belts. Granted, before the currency was created, governments strove to cut their deficits to 3% of GDP and to lower their debt towards 60%, the ceiling for new members. Now a stability and growth pact is supposed to keep deficits and debts down. Portugal is trying hard to cut spending, but big countries have done much as they please. Last year four members had deficits in excess of 3% of GDP; another's was 2.9%. Seven have debt ratios of more than 60% (see right-hand chart).

Arbitrary limits on government finances make little sense. But pact or no pact, Italy and others need to put their finances straight and raise their growth rates. Indeed, the two problems are linked. To the extent that slow growth hurts tax revenues, and thus the ability to service public debt, markets may begin to take a less benign view of slow growers' bonds. And the greater the debt, the more damage a change in market mood can do.

The bad news, and the bad news

Unfortunately, there is no easy way out. In a currency union, with devaluation ruled out, there are only two ways of reducing unit labour costs relative to those of other members. One is to put up with lower wage growth than the rest. This is possible—low wage growth has given Germany a route out of trouble after a miserable few years—but painful. Workers do not accept small wage increases, let alone cuts, easily; and slow wage growth adds little to domestic demand. The other option is to raise the rate of productivity growth, which looks no easier. Both Italy and Portugal have had poor productivity records, although the microeconomic reforms proposed by Italy's newish government are steps in the right direction. And businesses in these countries are not only competing against well-heeled Germans. They are also going head-to-head with Asians and central Europeans.

To salvage the public finances at the same time as restraining wages or pursuing microeconomic reform may seem to be asking too much. After all, it is at just such times that domestic demand could do with support from the state. But as Alberto Alesina and Francesco Giavazzi, two Italian economists, have argued, budgetary tightening, as long as it is based on spending cuts rather than higher taxes, may even boost demand, because citizens expect to have lower tax bills in the future. This seems to have been the experience of Ireland and Denmark in the 1980s.

Not everyone thinks as ill of Italy as the agencies. Eric Chaney, of Morgan Stanley, argues that Italian businesses are better placed than most commentators think. Even so, the spendthrift cannot afford to wait for economic growth to pull their debt burdens down. Should the markets show a little discrimination and discernment, and demand more interest for their money, life in the euro zone may become much less comfortable.

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Maternal nutrition

Recipe for averting disaster

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Omega-3 is very good for fetuses, especially those whose mothers have HIV

Alamy

YOU are what you eat, or so the proverb goes. If you happen to be a baby, though, you tend also to be what your mother ate when she was pregnant. Moreover, a breastfed baby is what his or her mother continues to eat.

For many years it has been known that maternal nutrition affects the development of the child. Eating folic acid, present in leafy green vegetables, ensures that the fetus has the nutrients it needs to grow the casing to the neural tubes that link the brain to the rest of the body. As a result, many pregnant women in the West take supplements that contain the nutrient.

In recent years the role of fatty acids such as omega-3, present in oily fish including salmon and sardines, has been identified as important in producing children who are bright, dextrous and sociable. Such is the effect that it overwhelms the disadvantage of ingesting the heavy metals that tend to accumulate in oily fish. Smart mothers-to-be in the rich world take plenty of these fatty acids.

Recent research presented this week at a meeting in London of the Letten Foundation shows just how important maternal nutrition can be. Indeed, a study from Tanzania and Zimbabwe shows that if a mother-to-be eats well, she may even be able to overcome the disadvantages her child will face if she carries the human immunodeficiency virus, HIV, that causes AIDS (except, of course, infection with the virus itself).

Tom Brenna of Cornell University in America has conducted research on how fatty acids, in particular, plant and animal forms of omega-3, are essential to the development of the brains of infants. He particularly stresses the importance of the animal form, called docosahexaenoic acid (DHA), present in oily fish and the eggs of hens fed seeds high in plant omega-3.

Food for thought

Dr Brenna's research shows that babies' brains start to be loaded with DHA at 25 weeks after conception,

a process that continues until they are two. Moreover, fetuses and infants process lots of essential fatty acids, including DHA, in ways other than those needed to build merely the brain. This suggests that the fatty acids' role is more complex, and possibly more important, than was thought. Dr Brenna reckons that DHA is so vital to developing brains that he is campaigning to get formula milk fortified with it.

For babies with problems, what their mothers eat is even more important. This is particularly true for babies whose mothers are infected with HIV, even when the virus is not passed from mother to child. Such infants are smaller and more likely to be premature than those whose mothers do not have the virus.

Jacqueline Uriyo of the Kilimanjaro Christian Medical Centre in Moshi, Tanzania, has conducted research which shows that HIV would appear to affect the developing brain. She tested the children born to 1,745 mothers who did not have HIV and 128 mothers who did have the virus. Of these children, 80 were uninfected, 11 were infected and a further 37 died or moved away before they were old enough to be tested at 18 months.

Dr Uriyo examined the mental development and dexterity of the infants at three, six, nine and 12 months. Of the 1,873 tested, 6.2% were identified as being at high risk of slow development. Previous research has shown that twins can fall into this category. But in this study, the children most at risk were those born to mothers with HIV. Indeed, says Dr Uriyo, the HIV status of the mother would appear to be more important than that of the child.

What might be done to reverse the damage? With Gwen Kandawazvika of the University of Zimbabwe, Dr Uriyo decided to try adding omega-3 to the diets of pregnant women. The pair gave supplements to small numbers of women with and without HIV while they were pregnant and for six months afterwards. They found that the performance of babies born to mothers with HIV improved, but faltered at nine to 12 months when the supplements stopped. Some caution is needed. The pilot study was too small for statistically significant conclusions to be drawn from it and was complicated by the combining of two different populations. But it does at least indicate that something may be done to help babies born to mothers infected with HIV.

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Climate change

Bubbling up

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A new experiment to test the role of cosmic rays in global warming

SIR WILLIAM HERSCHEL, an 18th-century astronomer, is credited with being the first person to notice the effect of variations in the sun's activity on the Earth. In 1801 he observed that when the sun had many spots on its surface, the price of wheat fell—a connection he attributed to the weather being more temperate. Over the next 200 years scientists tried, without much success, to understand exactly how these transient sunspots might affect the climate. Now an experiment has begun that could explain what is going on.

The Earth is continually bombarded by streams of particles that come from outside the solar system. These cosmic rays, as they are called, consist mostly of protons. They strike the gases of the Earth's atmosphere at great speeds, creating showers of debris including streams of electron-like particles called muons. An international team of physicists led by Jasper Kirkby, who works at CERN, the European particle physics laboratory near Geneva, has devised an experiment to find out how this process might affect the climate.

When scientists first turned their attention to subatomic particles, including cosmic rays, they used a device called a cloud chamber to study them. These are boxes containing air that is super-saturated with water vapour. When a charged particle zips through the chamber, the vapour condenses into a trail of droplets showing the particle's path and, if the box is placed in a magnetic field, its electrical charge.

In an updated version of a cloud chamber the researchers are recreating the Earth's atmosphere. They fill the container with pure air made by evaporating liquid nitrogen and liquid oxygen, and add water vapour and some trace gases. They adjust the temperature and pressure of the mix to mimic conditions at various heights above sea level. Then they zap the results with a stream of particles from the laboratory's elderly proton synchrotron. Ideally, they would use muons but, in practice, they are using a close cousin, the pion.

The theory is that when a muon encounters a gas molecule, it can knock off an electron, leaving a positively charged ion in its wake. The electron soon attaches itself to another molecule, making a negatively charged ion. These ions are thought to help create new particles called aerosols and, when aerosols grow above a certain size, they become the seeds around which cloud droplets form.

The experiment is testing this theory. If it is correct, then cosmic rays may create clouds with more small droplets than would otherwise be the case. Such clouds would persist for an unusually long time because small water droplets are less likely than big ones to turn into rain. Physicists also think that such clouds would be brighter and more reflective than normal clouds. So they would cool the Earth by hanging around and by reflecting more heat from the sun back into space.

The link between the sun's activity and climate involves another lot of particles streaming past the Earth. The planet and its neighbours are bathed in the solar wind, a stream of charged particles ejected from the upper atmosphere of the sun. The magnetic field associated with these particles helps protect the Earth from cosmic rays by deflecting them from the planet.

When the sun is at its most active, which is when it is spotty, the solar wind is stronger and fewer cosmic rays penetrate. Conversely, when solar activity is less intense, more cosmic rays get through. A study using data on cloud cover taken from satellite images dating from 1979 found that 65% of the world's skies were covered by cloud when cosmic rays were weakest and 68% when they were strongest.

Scientists modelling climate change have ignored cosmic rays up to now because there was not enough

evidence about how they might work. However, the results of this experiment, expected by summer 2007, could show how nature periodically sticks her oar in. The experiment on cloud formation also seems likely to undermine the particle physics laboratory's reputation for pursuing only blue skies research.

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About sponsorship

Cancer therapy

Choose your poison

Oct 26th 2006
From The Economist print edition

A new test picks the chemotherapy most suited to the tumour

CHEMOTHERAPY, used to treat cancer since the 1940s, is a blunt instrument. The drugs attack every rapidly dividing cell in the body. Cancer cells are destroyed but so too are cells that would be better kept alive, such as hair follicles and the cells that line the gut, the loss of which makes cancer patients bald and nauseous. Although several cancers can now be treated by drugs targeted directly at the tumour cells, in most cases a patient's survival depends on whether he dies from the side effects of chemotherapy before the chemotherapy kills the cancer, or vice versa. A way to pick the right type of chemotherapy would make a big difference.

Anil Potti and colleagues, of Duke University in North Carolina, have proven—in principle, at least—that they can do exactly that. Instead of prescribing chemotherapies according to a doctor's best guess, they propose a genetic analysis to predict which type of chemotherapy would stand the greatest chance of zapping cancerous cells.

Their method is based on finding a rough match between the genes that are activated in an individual's tumour and those that are typically busy in cancer cells when different chemotherapies perform at their best. As they explain in *Nature Medicine*, the more similar these two profiles, the more likely it is that a patient taking a drug will benefit from its tumour-destroying potential. The test could improve the prospects of patients who currently suffer the side effects of chemotherapies without knowing if they are undergoing a treatment that has a good chance of working for them.

The test differs from existing technologies in that it can pick between drugs for many cancers rather than just one. It correctly predicted the optimum drug from the six main chemotherapies used to treat three of the most common tumour types in 81% of tests. Since submitting the paper, the researchers say they have increased the number of chemotherapies to 15 and maintained the high accuracy. Clinical trials are under way.

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Photography

A pixel worth a thousand words

Oct 26th 2006
From The Economist print edition

A new type of camera that could detect explosives and other hidden items

SALESMEN flogging digital cameras boast of the number of pixels in the images captured as an indicator of quality. The more pixels there are—and they are usually counted in the millions—the better the picture.

That may cease to be the case. Scientists have devised a way to get the same quality using a single pixel. And it gets better—the new camera will need less memory and power, and may be able to capture images at wavelengths that could prove useful for airport security.

The trick is to manipulate the way in which the camera captures and stores information. Doing this involves a whole new branch of information theory developed just a couple of years ago, known as compressed sensing.

When a picture is taken with a digital camera that has, say, 1m pixels, the device momentarily captures 1m pieces of information. A computer chip inside the camera then immediately compresses this data, using a piece of mathematical wizardry called a Fourier transform. The information about the image is converted from 1m to about 10,000 numbers that correspond to the most important items of the mathematical transformation. It is these numbers that are stored to recreate the image; the rest of the data is ditched.

Richard Baraniuk and Kevin Kelly of Rice University in Houston, Texas, used compressed sensing to eliminate this waste. As the name suggests, it cuts the quantity of data required by using a new way to sense an object. The pair built a camera with just one pixel that captures many images over time and uses information from them to create a single picture. Instead of looking once at the object using a million pixels, it looks 10,000 times using one pixel.

The researchers, who reported their results at the Optical Society of America's annual meeting earlier this month in Rochester, New York, used a digital micromirror device, a piece of kit invented 20 years ago that is now commonly used in digital televisions and projectors. It contains several hundred thousand microscopic mirrors arranged in a rectangular array. The position of these mirrors can be altered millions of times per second. The mirrors appear either bright or dark, depending on the angle at which they are set. By changing these angles at random between their 10,000 closely spaced shots, the researchers captured enough information to create a high quality image.

Standard cameras process the information they capture to turn it into a picture. With the single-pixel camera, by contrast, a separate computer recombines information about the light levels with information about the patterns of the micromirrors to create an image. A commercial version of the camera would therefore need far less power than cameras that do their own computing, and its batteries would last far longer.

The new camera may have another big advantage over standard devices—the ability to capture images at terahertz wavelengths, which sit between the infra-red and microwave regions of the electromagnetic spectrum. These wavelengths can penetrate clothes, paper and plastic, so are useful for detecting hidden items. Handily, explosives and drugs have characteristic fingerprints in the terahertz range.

There is some way to go before the single-pixel camera appears in the shops. The prototype is as big as a coffee table and takes five minutes to capture enough images to generate a high quality picture. But the technology's potential uses may make bringing it to market worthwhile.

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Homosexuality

All creatures great and small

Oct 26th 2006
From The Economist print edition

How homosexuality, widespread in the animal kingdom, may have evolved

Getty Images

The birds and the bees

WHAT is taught in a country's schools reveals much about the national psyche. The Norwegian curriculum requires that all 14-year-olds learn about homosexuality. Assisting with this education, the National History Museum at the University of Oslo has just opened an exhibition of gay animals.

“Against Nature?” does not tell zoologists anything new. Homosexuality has been recorded in some 1,500 species so far, and been well documented in about a third of these cases; it has been known since the time of Aristotle, who thought he witnessed two male hyenas having sex with one another. But the exhibition's purpose is not to educate zoologists. It is to persuade the public that, as there are gay whales and worms, gay humans do not disturb the natural order.

Aside from illustrating homosexuality among an extraordinary variety of creatures, the exhibition shows how sexual stimulation can vary when, at first blush, the mechanical details of how this might work are not obvious to people attempting to draw analogies from their own anatomies. Male Amazonian river dolphins, for example, penetrate the blowholes of other males; female bottlenose dolphins use their snouts as dildos on other females.

Why this behaviour might be favoured by natural selection, though, is a difficult question to answer. In an attempt to do so, the exhibition picks on gay flamingos. Two males raising a chick after one of them had a one-night stand (of sorts) with a female are able to hold a larger territory than male-female partnerships. This suggests a chick with two dads could get more food and therefore have a better chance of survival. But explanations are harder when gay animals (such as some humans and, apparently, some killer whales) never try to mate with the opposite sex.

Theoretically, there are several possible ways homosexuality could have evolved. One is that homosexuals assist in the upbringing of their relatives so much that they pass on more of their genes this way than by having children themselves. Another suggestion assumes the genes that confer homosexuality in males are different from those that confer it in females. For the theory to work, these genes would have to confer some extra reproductive advantage to their straight carriers. This way, genes that increase the chances of one sex surviving and reproducing might not be discarded through the generations even though they inhibit making babies when they occur in the opposite sex. But testing these theories is hard, so nobody knows if they are true.

Taking lessons on sexuality from the birds and the bees itself requires first accepting something not taught ubiquitously outside Norway—that evolution occurs by natural selection.

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About sponsorship

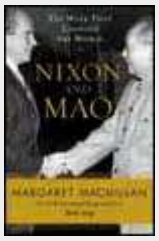
America and China

Grand vision and petty deceit when Nixon met Mao

Oct 26th 2006
From The Economist print edition

The first visit to China by an American president was notable, above all, for its symbolism. A new book analyses the characters involved and what they got from it

Seize the Hour: When Nixon Met Mao
By Margaret MacMillan



To be published in America as "Nixon and Mao: The Week that Changed the World" by Random House in February 2007
John Murray; 384 pages; £25.

Buy it at
Amazon.com
Amazon.co.uk

Corbis

RICHARD NIXON'S visit to China in 1972, stage-managed by his national security adviser, Henry Kissinger, was a diplomatic *coup de maître*. It all but guaranteed Nixon's re-election, transformed superpower politics, opened China to the outside world and dazzled the media. It has even been celebrated in an opera.

A third of a century later, however, the visit looks less bright than it did at the time. Nixon himself survived politically for little more than two years. More to the point, the gambit failed to relieve the pressure on America in Indochina, which was one of its chief purposes. Within three years, with Chinese

aid pouring in to help the Vietcong, America had suffered a humiliating defeat in Vietnam.

Nixon and Mr Kissinger tried to avoid betraying their ally, Taiwan, but could not resist making grand statements to impress their Chinese hosts. “There is one China,” Nixon told the Chinese prime minister, Zhou Enlai, at their first private meeting, “and Taiwan is part of China.”

Today China loudly asserts that Taiwan is indeed a part of China, but it manifestly is not governed as such. Though the fiction is observed, it is still a fiction. China remains a Communist state, albeit one that has embraced capitalism. Yet the American president's visit acknowledged that China was a great power, encouraged American companies to do business there and helped China in its relations with the Soviet Union. On balance, China gained more from the transaction than America.

Mr Kissinger was not good at economics. This was never more clearly shown than by his dismissive judgment that “the maximum amount of bilateral trade possible between us, even if we make great efforts, is infinitesimal in terms of our total economy.” Today America's trade deficit with China is running at about $215 billion a year, and America's debt to China is increasingly seen as a problem.

However mistaken many of the assumptions made by all four principals at the Beijing poker table—Mao Zedong, the dying emperor surrounded by pretty, scheming nurses, the urbane Zhou, grumpy Nixon and the neurotic Mr Kissinger—this was international politics on a grand scale. Margaret MacMillan, a Canadian historian whose masterly evocation of the Paris peacemakers of 1919 has been a bestseller on both sides of the Atlantic since it was published in 2001, has now done fitting justice to another great diplomatic episode.

With a sharp eye for the ironic and the bizarre, she describes the intrigues, the insults and the betrayals of her characters. Mr Kissinger, for example, preferred to use Chinese interpreters because they could be trusted not to talk to the American press. He handed over reams of classified American intelligence about the Soviet Union to its Chinese enemies. Ms MacMillan gives abundant examples of the spite with which he sidelined the secretary of state, William Rogers, who was kept ignorant of America's secret talks with the Chinese for over two years, until Mr Kissinger had returned from his first visit to Beijing. Yet Mr Kissinger's intelligence, and his excitement at the sheer scale of his undertaking, shine through the narrative.

Nixon emerges as an ungracious figure, but also as the original architect of the whole daring project. He also comes across as a shrewd analyst of the great game. Some of the most revealing discoveries Ms MacMillan has made in her researches are the haiku-like memos Nixon wrote on his yellow pads. One, which he scribbled before the talks started, begins:

What they want:

1. Build up their world credentials
2. Taiwan
3. Get out of Asia

What we want:

1. Indo China (?)
2. Communication—To restrain Chinese expansion in Asia
3. In future—Reduce threat of confrontation by China Super Power

What we both want:

1. Reduce danger of confrontation & conflict
2. A more stable Asia
3. A restraint on USSR

The question-mark against Indochina alone deserves a volume of explanation. This is a great story, entertainingly told.

Seize the Hour: When Nixon Met Mao.
By Margaret MacMillan.
John Murray; 384 pages; £25.
To be published in America as “Nixon and Mao: The Week that Changed the World” by Random House in

February 2007

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About sponsorship

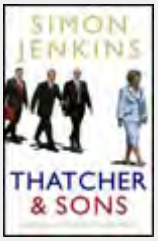
Thatcherism

The centre holds—all too well

Oct 26th 2006
From The Economist print edition

SIR SIMON JENKINS is a prolific and wide-ranging commentator. He writes elegantly and his opinions are trenchant. In this book, however, his thesis manages to be both familiar and not quite right.

Thatcher & Sons: A Revolution in Three Acts
By Simon Jenkins



Penguin/Allen Lane; 375 pages; £20

Buy it at
Amazon.com
Amazon.co.uk

Sir Simon believes that while successfully seeing through one revolution, in which market economics routed socialism and transformed Britain's ability to compete, Margaret Thatcher also made another revolution—an unprecedented centralisation of state power. The effects of this have been far less happy. To Sir Simon, though, the most curious aspect of Mrs (now Lady) Thatcher's double-edged achievement has been the way her successors, John (now Sir John) Major and, in uneasy partnership, Tony Blair and Gordon Brown, have not just secured both revolutions, but in many ways extended them.

Sir Simon depicts Mrs Thatcher as an archetypal charismatic leader who is unconstrained by traditional loyalties and has no compunction in breaking institutions that represent countervailing power. Though her vision is of a people liberated by the benign hand of the market to forge their own destinies, the only way she can realise it is by ruthless centralisation.

To that end, it was not only Britain's overweening trade unions that had to be crushed. Others, too, had to be bent to Mrs Thatcher's will, including a professionally sceptical civil service, those professional bodies that had become resistant to the change so constantly imposed from above, the quasi-autonomous universities, a hidebound criminal-justice system and, most tiresome of all, Britain's bolshie local councils, especially those of a socialist bent that challenged her directly.

Albeit without any great new insights, Sir Simon chronicles this paradox at the heart of Thatcherism with verve and telling illustration. Where he is on much shakier ground is in his assertion that the “sons” who came after her were more Thatcherite than the Iron Lady herself. That Mr Major undertook further privatisations and market-led reform of public services is hardly surprising: he was, after all, Mrs Thatcher's chosen successor. The Tories got rid of her because they were fed up with the woman, not, with the exception of the poll tax, her policies.

As for Mr Blair and Mr Brown, they pragmatically understood that the only way for Labour to win office again after 18 years was by promising not to undo the best bits of the Tories' economic legacy. But both Mr Blair and Mr Brown have a commitment to social justice that is entirely alien to Mrs Thatcher. Mr Brown may have left the top rate of marginal tax unchanged, but he has seized every other opportunity to raise the overall burden of taxation for redistributive ends. Mr Blair, belatedly, came to believe that breaking up the monopoly provision of public services was essential if they were to respond to the high expectations of a consumer society. But it is inconceivable that Mrs Thatcher would have approved of Mr Blair's decision to preside over a near-doubling of spending on the health service. Her approach was to raise spending on health by just enough to prevent the NHS from electorally disastrous collapse. Nor would Mrs Thatcher have dreamed of devolving power to Scotland and Wales, as Labour has done.

Sir Simon is on firmer ground in his analysis of the baleful influence of an imperial Treasury. More than anything, the thread that links Thatcherism with New Labour in office is the supremacy of the Treasury. Through its attempts to keep tabs on every pound spent by the state, it has become the instrument of Britain's centralisation. Thanks in part to the deal over the prime ministership struck by Mr Blair and Mr Brown in 1994, the Treasury has become even more formidable under New Labour—a trend unlikely to be reversed when Mr Brown moves to Number 10.

Sir Simon hopes for a third revolution, in which what is known as the “new localism” asserts itself and political decisions are taken at the level closest to those affected. Perhaps a prime minister will come along as determined to do something about this as Mrs Thatcher was to reverse Britain's economic decline. Perhaps.

Thatcher & Sons: A Revolution in Three Acts.
By Simon Jenkins.
Penguin/Allen Lane; 375 pages; £20

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About sponsorship

The United Nations

Behind the scenes

Oct 26th 2006
From The Economist print edition

HAS Kofi Annan saved the United Nations, or merely slowed its slide into irrelevance? James Traub does not pretend to give scholarly answers to such questions; he is too unashamedly partisan for that. He does nothing to hide his respect and affection for Mr Annan, the “kindly African with a silver goatee and rueful yellowing eyes...the most gracious of men”, whose ten years as secretary-general end on December 31st. Nor does he disguise his admiration for the UN, that “beautiful illusory empire of good intentions”, though he is not blind to its many failings.

The Best Intentions: Kofi Annan and the UN in the Era of American World Power
By James Traub

Farrar, Straus and Giroux; 464 pages; $26.
Bloomsbury; £20

Buy it at
Amazon.com
Amazon.co.uk

But this does not detract from the book. On the contrary. The very mention of the UN tends to make people yawn, but Mr Traub brings it to life with a highly readable account of the infighting and drama that have gone on behind the scenes over the past 15 years, along with often amusingly acerbic thumbnail sketches of several prominent characters. In addition to making use of his many articles for the *New York Times* and other publications, he has drawn on what he learnt during the year he spent as a fly-on-the-wall observer at Mr Annan's side, during which he conducted hundreds of interviews with him and his staff, without, he says, any restrictions on what he could report.

Mr Annan emerges from all this very much as he seems in public—a competent, self-effacing, gentle man with great charm and a genuine horror of violence, but who lacks the thick skin and inner strength required to push through essential reforms or to deal with the many crises that have beset the UN on his beat. He has not proved a fighter. Lionised during his first term—he won the Nobel peace prize in 2001—he has been dogged in his second by the Iraq war, a scandal concerning the oil-for-food programme in Iraq and another involving sexual abuse by UN peacekeepers. Through his son's actions, he himself has been accused of impropriety.

For all his good intentions, Mr Annan has failed to provide the leadership required at the hour of the organisation's need. Whether his successor, Ban Ki-moon, will be able to do any better is open to doubt. As Mr Traub points out, in the end the secretary-general has little power. It is the Security Council—or rather its five veto-wielding permanent members—who ultimately call the shots.

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By James Traub.
Farrar, Straus and Giroux; 464 pages; $26.
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About sponsorship

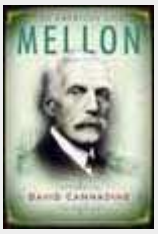
Andrew Mellon

Made it, bought it, ran it, gave it

Oct 26th 2006
From The Economist print edition

OF ALL America's great men, Andrew Mellon is arguably the least-known and most under-appreciated. Yet the life of this banking tycoon, politician and philanthropist was remarkable, and its impact on his country wider and far more beneficial than those who know of him generally believe. And it is a life that deserves to be studied more than ever, since so much of it raised issues that are relevant today.

Mellon: An American Life
By David Cannadine



Knopf; 743 pages; $35.
Penguin/Allen Lane; £30

Buy it at
Amazon.com
Amazon.co.uk

"It was a different time from ours. Or was it?" asks David Cannadine nearly half way through his superb biography of a man whose story prompts that question many times over. Mellon was one of America's richest men during the roaring 1920s, that gilded age to which today's increasingly unequal society is often compared. The debate that raged during his lifetime over the relationship between inequality and wealth-creation, and the responsibility of the rich winners to poorer folk, still rages today, though America now offers some mechanisms for redistribution and a social safety-net of kinds, both strongly opposed by Mellon.

His business empire, which combined huge industrial enterprises such as Gulf Oil and the aluminium giant, Alcoa, with a powerful bank, Union Trust, was privately held. It resembled, in a purer and family-owned form, today's increasingly powerful private-equity firms, such as Kohlberg Kravis Roberts and the Blackstone Group. But Mellon was more than a mere shareholder in blue-chip businesses or a supplier of loans to them. He was the leading, risk-taking, venture capitalist in Pittsburgh, the Silicon Valley of its day.

During the burst of industrialisation between the 1860s and 1920s that transformed America into the world's leading economic power, Pittsburgh led the way. It was the home of Andrew Carnegie, Henry Frick, George Westinghouse and Henry John Heinz, as well as Mellon. The "Mellon system" involved identifying new industries, often by backing research that led to scientific breakthroughs, and then vertically integrating these businesses under a dominant company. As Mr Cannadine notes, although a believer in the market, Mellon, like many businessmen of the time, also "rather liked monopolies". Mr Cannadine finds no evidence to support the widely believed story that Mellon turned down the chance to back the young Henry Ford. But he might have done so, had the opportunity arisen: he had an eye for an invention.

Mellon's belief in free enterprise, self-reliance and the virtues of inequality owed much to the combination of his strict Presbyterian Ulster heritage and his powerful father, Thomas "the Judge" Mellon. This helped him succeed in business, but let him down in both his personal and his public life. According to Paul Mellon, in his memoir "Reflections in a Silver Spoon", his father Andrew entered adulthood as a "thin-voiced, thin-bodied, shy and uncommunicative man". According to one contemporary, he was so closed that, had he got religion, he would not have "told it to God". He broke off an engagement, on his father's orders, after discovering that his fiancée was dying of consumption. When he did marry, it was in his 40s to a wholly unsuitable girl from England, "his one open rebellion against his father and his family". The marriage, which Mr Cannadine likens to that of Prince Charles and Lady Diana Spencer, soon ended in scandalous divorce—not surprisingly, as Mellon treated his needy young wife "like a client at the bank, seeking a loan to finance an ill-conceived venture". His relations with his children were also blighted.

Mellon's beliefs may also account for the disastrous end to his career as treasury secretary, a post now held again by one of the country's richest bankers. Mellon took the job reluctantly aged 65, and pioneered the supply-side reforms still favoured by some today. He wrote a best-selling book, "Taxation: The People's Business", which argued that cutting tax rates for the rich would increase their revenue

(familiar?), and that many more people should be entirely exempted from paying federal income tax. When his reforms were (mostly) implemented, in 1926, he was vindicated: a man earning $3,000 a year paid no income tax, compared with $40 in 1920, and yet the rich did indeed pay more overall.

As treasury secretary, Mellon secretly continued to run his business empire with his brother Dick, despite publicly stating that he had severed all links with it, a conflict of interest beside which any relationship between Dick Cheney and Halliburton seems trivial. Despite this, and despite persistent allegations that his failure to enforce Prohibition effectively may have owed something to his past ownership of a distillery, by 1929 Mellon was regarded with a degree of admiration nowadays reserved for people like Alan Greenspan at his zenith as chairman of the Fed.

Yet when boom led to crash and then the Depression, the same instincts that had made Mellon a fierce opponent of trade unionism made him unsympathetic to the plight of the millions of unemployed workers. Instead of helping, he preferred to weather the economic storm confident that before long things would improve, as they always had in the past. He soon became a hate figure, and was shipped off as ambassador to Britain, where he devoted his time to increasing his collection of great art and successfully lobbying the British to sign over their oil rights in the Middle East to Gulf Oil.

As soon as Franklin Roosevelt became president, he set out to make Mellon a prime example of the “great promoter or the financial Titan” whose day he intended to ensure was past. Mellon was accused of tax fraud, and in his early 80s had to endure a humiliating trial, which exonerated him only after his death. In fact, during his life Mellon paid far more in tax than he needed to, says Mr Cannadine, who also finds not a “shred of evidence” that the gift of his art collection to the nation was part of a secret deal connected with the tax trial. Mellon had, it is now clear, been planning to create the National Gallery of Art since his time as treasury secretary, when he was also overseeing the design and construction of Washington's magnificent neo-classical Federal Triangle.

Mellon's philanthropy has echoes today. It is not so much that giving by the rich is fashionable again; rather it is that at least some acts of generosity are carried out without much self-aggrandisement. Mellon did not insist on his name adorning the National Gallery, an act of self-effacement that was not surpassed by any philanthropist until this year, when Warren Buffett chose to give most of his fortune to the Bill & Melinda Gates Foundation rather than create one of his own.

Mellon: An American Life.
By David Cannadine.
Knopf; 743 pages; $35.
Penguin/Allen Lane; £30

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New fiction

Insipid and overcooked

Oct 26th 2006
From The Economist print edition

COMMERCIAL expectations will be high for “Thirteen Moons”, Charles Frazier's first novel since his bestselling debut “Cold Mountain”. So Random House must have been heartened that Mr Frazier's new book entered the *New York Times* bestseller list at number two. But sometimes there is no clever way to say it: “Thirteen Moons” is awful.

“Cold Mountain” was a clever book and by loosely basing Will Cooper, the narrator of this latest tale, on a fascinating frontiersman, William Holland Thomas, as Mr Frazier has done, this novel might perhaps have turned out just as well. So it is a puzzle that he could render such a compelling life story in a manner so dull. But then the finest ingredients can turn to overcooked mush in the hands of a cackhanded chef.

Thirteen Moons
By Charles Frazier

Random House; 420 pages; $26.95.
Sceptre; £17.99

Buy it at
Amazon.com
Amazon.co.uk

In the early 19th century the orphaned Will is a “bound boy” compelled to run a trading post in North Carolina's Cherokee Nation. At 13, he wins young Claire in a card game, and with the briefest of introductions is smitten. Although for most of the story the two are parted, Will's pining for his true love should provide the novel with its narrative drive. But the gearbox is stuck in neutral, and the narrative merely coasts. Claire has no character. Since Will has none either, they are perhaps perfectly suited. Yet the double absence makes it impossible to care whether these two ciphers will, or will not, in the end get together as one glorious nullity.

In long-winded, folksy prose, Will relates how he became an honorary Indian, a Great White Chief determined to protect a preserve for the Cherokee east of the Mississippi, even as President Andrew Jackson drives all Indians west of the river, an expulsion that infamously resulted in the 1838-39 Trail of Tears. (Readers will be embarrassingly unmoved.) To create this preserve, Will amasses great tracts of land whose ownership is precariously perched on dodgy deals and promissory notes, and eventually the entire venture collapses.

Stuffed like a taxidermy project with lifeless details scooped from the books listed in the Author's Note (for example, “Cherokee Dance and Drama”), “Thirteen Moons” is a rather heavy volume to throw across the room. Best let the bookshops stow their stocks safely on the front tables that Random House will have so bounteously paid for.

Thirteen Moons.
By Charles Frazier.
Random House; 420 pages; $26.95.
Sceptre; £17.99

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About sponsorship

Dance

Overstretch

Oct 26th 2006 | BERLIN
From The Economist print edition

William Forsythe, an American choreographer, takes on the Iraq war

IN THE arts Germany is jumpy at the moment. Even in a country where theatre-makers have long prided themselves on tackling big political themes—this, after all, is the land of Schiller and Brecht—intolerance seems to be on the march.

At the Deutsche Oper in Berlin a production of Mozart's “Idomeneo” was recently cancelled for fear of putting the theatre and its public at risk from an Islamist bomb. Ending the opera with the King of Crete coming on with the head of Muhammad was deemed too dangerous. In Frankfurt “The Last Virgin”, a play about Palestinian suicide-bombers by a Jewish writer, Tuvia Tenenbom, finished with a bomber pleading for the Jews to leave the Middle East altogether. It caused outrage in the local Jewish community.

One artist, however, William Forsythe, an American choreographer, is not afraid to tackle the war in Iraq, an issue that is certainly controversial in his own country. Mr Forsythe has worked as a dancer and choreographer in Germany for over 30 years. For two decades, until it folded in 2004, he ran Ballett Frankfurt, one of Europe's most adventurous dance troupes. Never overtly political, Mr Forsythe's work has nonetheless tackled such topics as sexuality, alienation and violence.

His latest dance piece, “Three Atmospheric Studies”, was created to inaugurate his new troupe, the Forsythe Company. The Sadler's Wells Theatre in London, where the piece ran for four nights earlier this month, trailed it as “the most damning comment on the horror in any art form since the Iraq war began”.

Mr Forsythe makes no such claims. But it is clear, from one of the characters' opening announcement, “My son was arrested,” to the crashing and explosions that threaten to overwhelm part three's more sensitive choreographic action, that this is as vivid a depiction of the mayhem of war, and the vulnerability of human bodies, as any work of contemporary dance dare be.

A model for “Three Atmospheric Studies” is Lucas Cranach's 1503 painting of the crucifixion: a mother mourns her lost son. At the start dancers—running, falling, sliding—enact confusion. Who is chasing whom? Who is fleeing whom?

In the second “study” the mother seeks her arrested son via an obstreperous interviewer, who takes her story down in Arabic. Between them someone tries to explain what is going on. Maybe he is reading the news. He could be Cranach. He could be a Middle Eastern television anchor.

Mr Forsythe has always worked with text and his techniques here are deliberately oblique and defiantly non-balletic: “I am a citizen,” he says. “It is my right to speak. In this piece I want to look at freedom of speech, and at how governments manage the frame and change the ground as war proceeds.”

This is uppermost in part three of the performance, when a woman walks amid a swirl of dancers, some smashing into walls, telling an unnamed “Ma'am” that there is “no cause for alarm”. Her voice, by turns plaintive and coaxing, is distorted to resemble a man's. This could be Donald Rumsfeld or any government representative trying to explain away the destruction wrought by military violence.

As a piece of dance, the unfriendliness of “Three Atmospheric Studies” will baffle some. As a piece of political art, it may cause anger, or mere indifference. Aesthetically, however, it packs a huge punch and, unusually for choreography, leaves one feeling anxious, unsure as to what has just been witnessed.

Mr Forsythe feels this is the right response: “It's hard to give the piece a name. I'm glad about that. You don't go to the theatre just to see what you know. And yes, it is a form of dissent. I read a lot of newspaper editorials. I'm certain that what I've done is no more scathing than anything I've read. ‘Three Atmospheric Studies’ is definitely not agitprop.” Maybe not. But it is definitely political.

The Forsythe Company is touring with “Three Atmospheric Studies” to the Schauspielhaus, Zurich (November 2nd-6th); then to Cal Performances at the University of California, Berkeley (February 22nd-23rd); then to the Brooklyn Academy of Music, New York (February 28th-March 3rd); and lastly to De Singel, Antwerp (May 30th-June 1st). Further information is available by going to www.theforsythecompany.de or by telephoning +49 (0) 69 21 23 75 86.

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About sponsorship

Eric Newby

Oct 26th 2006
From The Economist print edition

Eric Newby, travel writer and fashion buyer, died on October 20th, aged 86

BY THE standards of many British explorers, Eric Newby was not particularly intrepid. He could not bear the thought of pain, and would faint away in any film that featured an operating theatre. Horses terrified him, especially when, in Italy, a reluctant mare he was riding was persuaded to clear a ditch by having a lighted cigarette inserted up its backside. Forced to sleep on rocks—to Wilfred Thesiger's huge disdain—he would blow up an air-bed to cushion the ordeal.

But then Mr Newby did not see himself as an explorer in the Thesiger mould. He was a traveller to whom things happened, and he would set off in that inquiring, ill-prepared, innocent way that has characterised Englishmen abroad from Chaucer to Evelyn Waugh. He was an amateur whose 25 travel books—most famously “A Short Walk in the Hindu Kush” (1958) and “Love and War in the Apennines” (1971)—were full of serendipity and surprise. A sudden view of a ravine with a grey heron winging across it; the moon rising “like a huge rusty coin”; Parmesan cheese, eaten after days of hunger, with “hard, salty nodules” of curd in it; the shock of blue and green phosphorescence dripping from his oar. Possibly only Mr Newby could notice, while treading water off the east coast of Sicily in 1942 and trying to avoid being shot at by Germans, that the plume of smoke over Etna looked like the quill of a pen stuck in a pewter ink-pot.

Well-equipped he may seldom have been, but he was usually well-dressed. For Mr Newby had another life. For 20 years, to finance his travelling and writing, he worked in the garment trade. After helping run the family firm of Lane and Newby Ltd, Wholesale Costumiers and Mantle Manufacturers, he joined the John Lewis Partnership in the Intelligence Department, meaning that he checked whether trousers fitted or not. After this, he was promoted to “Model Gown Buyer”. If this life of pins and patterns seemed a come-down to a man dreaming of the Ganges or the Sahara, he certainly did not admit to it. To make “The Journey” as a sales rep through industrial Britain, rattling north overnight unsleeping in a third-class seat and then staggering up the back stairs of department stores with wicker baskets full of suits, was every bit as exciting.

Besides, he loved clothes. He had been drawn to travel in the first place, as a restless child growing up in suburban south-west London, by the pictures of foreign boys in petticoats in Arthur Mee's “Children's Colour Book of Lands and Peoples”. His first unaccompanied journey, following a Devon stream down to the sea through nettles and cowpats at the age of five, was made in brown lace-up shoes and “a hideous red and green striped blazer with brass buttons”. Apprenticed at 18 on a four-masted barque that ran the last great Grain Race from South Australia to Ireland, he first ran up the oily rigging, teetering 160 feet above Belfast, in grey flannel trousers and a Harris tweed jacket.

Melons and Sancerre

All this sounded rather upper class. And Mr Newby cut such a figure, handsome in immaculate safari suits and, in London, a trilby hat. He had a gentleman's cavalier attitude to expenses when, from 1964-73, he was the travel editor on the *Observer*, and a gourmet's approach to his later journeys. (“Had a delicious mini-picnic under a tree,” he noted during a bicycle ride through France in 1971; “small, ripe, melons and a bottle of cold Sancerre.”)

Yet he himself was “middle-middle class”. He had been to St Paul's, not Eton, and had left school at 16 because his family could no longer afford it. His time as a prisoner-of-war, from 1942 onwards, was diverting to him not only because it led him to his future wife (a tall, blonde, determined Slovenian girl who came to visit him when he was transferred to an outside hospital) but also because he could observe those strange creatures, the English upper classes, up close. Before that he had mostly met them in Harrods, small boys like him braving the “unending, snowy-white wastes” of the Linen Hall and the “savannahs” of Model Gowns, “endless expanses of carpet with here and there a solitary creation on a stand rising above it, like lone trees in a wilderness.”

In his travelling life he had many a narrow escape. On the great Grain Race, he was almost washed away in a hurricane. Hunting with princes in Andhra Pradesh he was charged by a bear, but failed to shoot it because he dared not use a rifle (a .465 Holland & Holland India Royal) that had cost £800. In Italy during the war, a fugitive prisoner, he woke from a sleep on a mountainside to find a German officer standing over him. But the officer wanted merely to chat and catch butterflies. “The last I saw of him”, he wrote, “was running across the open downs with his net unfurled...making curious little sweeps and lunges as he pursued his prey.”

Mr Newby was often asked why he loved to travel. It was, he said, to do with being free. But his attitude to freedom could be ambivalent. Twice, when he had got out of prisoner-of-war camps, he found himself musing that “real freedom” lay back inside the fence. There was no need, he wrote, to worry about anything there: no need to work, to earn money, or to think about what to eat. Or, indeed, what to wear.

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Overview

Oct 26th 2006
From The Economist print edition

America's Federal Reserve held its benchmark interest rate at 5.25%, extending its pause for a third month after two years of step-by-step tightening. The Fed said that the economy seems "likely to expand at a moderate pace", but added that "some inflation risks remain."

America's housing market cooled further. The median house price fell by 2.2%, to $220,000, in the year to September, according to the National Association of Realtors. It was the second monthly fall in a row. Activity was also lower than a year ago. Sales of existing homes fell for the sixth consecutive month, dropping by 1.9% in the year to September. Mortgage applications increased by 0.5% during the third week of October, according to the Mortgage Bankers Association. The demand for loans to buy homes had eased, but has bounced back a bit after a decline in the cost of borrowing.

Consumer prices in **Canada** declined, because the price of petrol dropped. Annual inflation fell to 0.7% in September, down from 2.1% the month before. Core prices, excluding those of food and energy, rose by 1.6% on the year.

The immediate industrial outlook in the **euro area** is still good. New orders rose by 3.7% in August, more than expected. That left them 14.3% higher than a year before, thanks to higher demand for transport equipment and metal products.

Spirits were lifted in **Germany**. The Ifo business-climate index rose for the first time in four months in October, to 105.3 from 104.9 the month before. French businessmen were also feeling brighter. The INSEE index, which tracks their mood, rose to 108 in October from a revised 106 in September. The unexpected increase was due to higher exports and production.

Britain's economy grew by 0.7% in the third quarter, beating expectations and matching the second quarter's pace. In the year to the third quarter, growth was 2.8%, raising expectations that interest rates may be increased soon.

A weaker yen bolstered **Japanese** exports, widening the country's trade surplus to $8.5 billion in September, 6.9% more than a year earlier. Exports to America went up by 20.4% and those to China by 19.8%, thanks to rising demand for cars and electronics.

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Output, demand and jobs

Oct 26th 2006
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2006	2007	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 1.9	Q2	+ 1.3	+ 2.7	+ 3.2	– 1.0	Q1	+ 3.6	Q2	4.8	Sep	5.1
Austria	+ 3.0	Q2	+ 3.6	+ 2.6	+ 2.0	+ 7.9	Jul	+ 2.2	Jul	4.8	Sep	5.2
Belgium	+ 2.8	Q2	+ 3.1	+ 2.6	+ 2.0	+10.7	Aug	+ 1.6	Jul	13.0	Sep†	13.5
Britain	+ 2.8	Q3	+ 2.8	+ 2.6	+ 2.4	+ 0.7	Aug	+ 3.2	Sep	5.5	Aug‡	4.7
Canada	+ 2.9	Q2	+ 2.0	+ 2.9	+ 2.6	+ 0.7	Jul	+ 3.7	Jul	6.4	Sep	6.7
Denmark	+ 2.8	Q2	+ 6.5	+ 2.7	+ 2.1	+ 4.3	Aug	+ 3.8	Aug	4.2	Sep	5.5
France	+ 2.6	Q2	+ 4.9	+ 2.3	+ 2.0	+ 1.0	Aug	+ 3.6	Aug	9.0	Aug	9.9
Germany	+ 2.4	Q2	+ 3.6	+ 2.3	+ 1.3	+ 7.3	Aug	+ 1.0	Aug	10.6	Sep§	11.7
Italy	+ 1.5	Q2	+ 2.2	+ 1.6	+ 1.2	+ 3.5	Aug	– 0.7	Jul	7.0	Q2	7.8
Japan	+ 2.5	Q2	+ 1.0	+ 2.8	+ 2.1	+ 5.9	Aug	+ 0.3	Aug	4.1	Aug	4.3
Netherlands	+ 2.8	Q2	+ 4.8	+ 2.7	+ 2.2	+ 2.7	Jul	+ 4.6	Jun	5.6	Sep††	6.6
Spain	+ 3.7	Q2	+ 3.8	+ 3.5	+ 2.8	+ 5.0	Aug	+ 4.1	Aug	7.8	Aug	8.6
Sweden	+ 5.1	Q2	+ 5.4	+ 4.4	+ 3.0	+ 7.0	Aug	+ 8.0	Aug	4.9	Sep†	5.4
Switzerland	+ 3.2	Q2	+ 3.0	+ 3.0	+ 2.0	+ 4.3	Q2	+ 4.5	Aug	3.1	Sep†	3.6
United States	+ 3.5	Q2	+ 2.6	+ 3.4	+ 2.4	+ 5.6	Sep	+ 4.8	Aug	4.6	Sep	5.1
Euro area	+ 2.7	Q2	+ 3.8	+ 2.5	+ 1.8	+ 5.4	Aug	+ 2.4	Aug	7.9	Aug	8.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 6.6	Q2	+ 7.6	na	na	+ 7.6	Aug	+ 5.5	Aug	7.9	Sep	8.3
Greece	+ 4.1	Q2	na	na	na	+ 2.3	Aug	+10.7	Jul	8.8	Q2	9.6
Iceland	+ 2.8	Q2	na	na	na	na		na		1.2	Aug†	1.8
Ireland	+ 5.0	Q2	+ 3.6	na	na	+ 5.5	Aug	+ 5.5	Aug	4.4	Sep	4.4
Luxembourg	+ 5.4	Q2	na	na	na	– 2.7	Jun	+ 2.3	Aug	4.1	Aug	4.1
New Zealand	+ 1.6	Q2	+ 1.7	na	na	+ 0.5	Q2	+ 0.9	Q2	3.6	Q2	3.7
Norway	– 0.5	Q2	+ 1.9	na	na	– 2.7	Aug	+ 5.0	Aug	3.0	Aug**	4.8
Portugal	+ 0.9	Q2	+ 3.8	na	na	+ 5.1	Aug	+ 2.5	Aug	7.3	Q2†	7.2

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡Jun-Aug; claimant count rate 3.0% in Sep.
§EU harmonised rate 8.5% in Aug. ††Jul-Sep. **Jun-Aug.

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Prices and wages

Oct 26th 2006
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2006	2007	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 3.9	Q3	+ 3.0	+ 3.4	+ 2.8	+ 7.9	Q3	+ 6.2	+ 4.7	Q2	+ 5.8
Austria	+ 1.4	Sep	+ 2.4	+ 1.8	+ 1.7	+ 2.4	Sep	+ 1.5	+ 2.7	Sep	+ 2.3
Belgium	+ 1.2	Sep	+ 3.2	+ 2.0	+ 1.9	+ 5.9	Aug	+ 1.7	+ 2.1	Jul	+ 2.5
Britain	+ 2.4	Sep*	+ 2.5	+ 2.3	+ 2.2	+ 1.8	Sep	+ 3.3	+ 4.2	Aug†	+ 4.1
Canada	+ 0.7	Sep	+ 3.4	+ 2.4	+ 2.2	+ 3.6	Aug	− 0.3	+ 1.4	Jul	+ 0.4
Denmark	+ 1.5	Sep	+ 2.4	+ 2.0	+ 2.0	+ 2.6	Sep	+ 5.3	+ 3.2	Q2	+ 2.9
France	+ 1.2	Sep	+ 2.2	+ 2.0	+ 1.7	+ 3.9	Jul	+ 3.3	+ 3.1	Q2	+ 3.0
Germany	+ 1.2	Oct	+ 2.3	+ 1.8	+ 2.3	+ 3.0	Sep	+ 3.6	+ 0.8	Aug	+ 0.9
Italy	+ 2.4	Sep	+ 2.0	+ 2.2	+ 2.0	+ 6.6	Aug	+ 3.7	+ 3.0	Sep	+ 3.1
Japan	+ 0.9	Aug	− 0.3	+ 0.3	+ 0.5	+ 3.6	Sep	+ 1.8	− 0.6	Aug	− 2.7
Netherlands	+ 1.1	Sep	+ 1.8	+ 1.6	+ 1.7	+ 4.9	Aug	+ 5.1	+ 2.0	Sep	+ 0.8
Spain	+ 2.9	Sep	+ 3.7	+ 3.8	+ 3.0	+ 4.2	Sep	+ 5.4	+ 3.1	Q2	+ 3.4
Sweden	+ 1.5	Sep	+ 0.6	+ 1.4	+ 1.9	+ 3.6	Sep	+ 4.2	+ 2.5	Jul	+ 2.9
Switzerland	+ 0.8	Sep	+ 1.4	+ 1.3	+ 1.3	+ 2.5	Sep	+ 1.5	+ 1.0	2005	+ 0.9
United States	+ 2.1	Sep	+ 4.7	+ 3.5	+ 2.4	+ 0.9	Sep	+ 6.9	+ 4.0	Sep	+ 2.7
Euro area	+ 1.7	Sep	+ 2.6	+ 2.2	+ 2.1	+ 5.7	Aug	+ 4.0	+ 2.4	Q2	+ 2.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.5	Sep	+ 1.2	na	na	+ 5.9	Sep	+ 3.8	+ 2.9	Q2	+ 3.7
Greece	+ 2.9	Sep	+ 3.9	na	na	+ 6.7	Aug	+ 5.5	na		na
Iceland	+ 7.2	Oct	+ 4.6	na	na	+11.9	Oct	+ 4.2	+10.6	Aug	+ 6.7
Ireland	+ 4.0	Sep	+ 3.0	na	na	+ 0.9	Aug	− 1.1	+ 4.1	Q2	+ 3.5
Luxembourg	+ 2.4	Sep	+ 2.9	na	na	+ 9.3	Aug	+ 5.4	+ 2.4	Jul	+ 0.9
New Zealand	+ 3.5	Q3	+ 3.4	na	na	+ 7.8	Q2	+ 4.7	+ 3.3	Q2	+ 2.6
Norway	+ 2.6	Sep	+ 2.0	na	na	+ 5.0	Sep	+17.9	+ 3.6	Q2	+ 3.8
Portugal	+ 3.0	Sep	+ 2.8	na	na	+ 4.3	Sep	+ 4.5	+ 1.1	Aug	+ 0.5

*RPI inflation rate 3.6% in Sep. †Jun-Aug.

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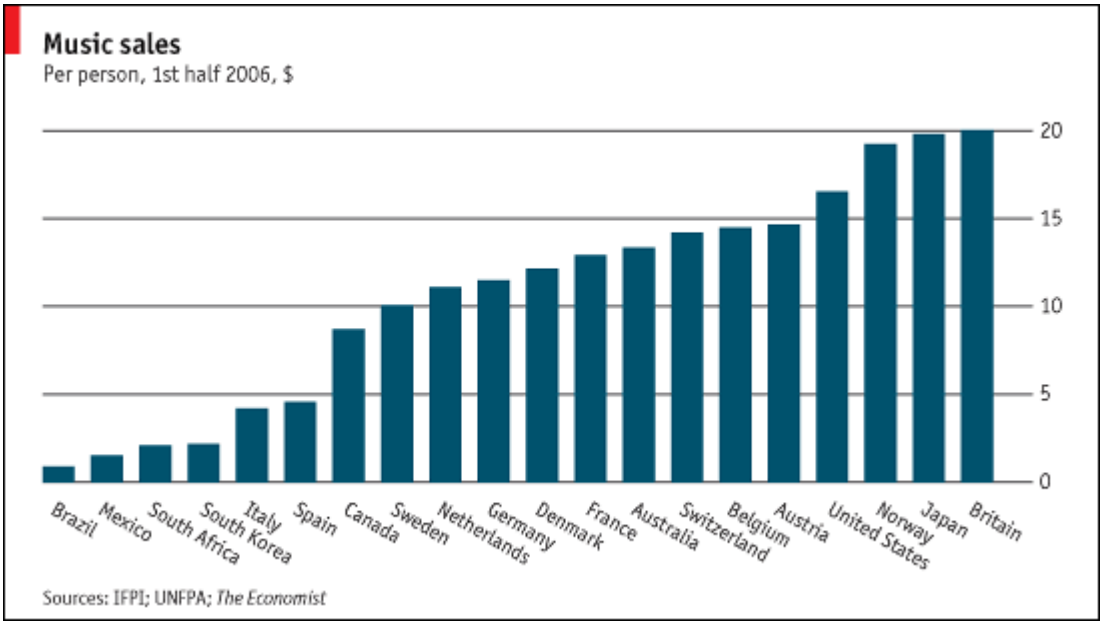
Music sales

Oct 26th 2006
From The Economist print edition



Not surprisingly, America is the world's biggest music market, with retail sales of $4.9 billion in the first half of the year. However, Britain, Japan and Norway, which is only the 19th-biggest market, buy more music per person. Rich does not necessarily mean big: Brazil, with sales of $163m, Mexico, with $162m, and South Africa, with $98m, all make the top 20 by absolute size.

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Money and interest rates

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	Money supply* % change on year ago			Interest rates % p.a. (Oct 25th 2006) 3-mth money market		2-year gov't bonds	10-year gov't bonds		corporate bonds
	narrow	broad		latest	year ago		latest	year ago	
Australia	+10.2	+11.2	Aug	6.32	5.66	6.14	5.78	5.48	6.94
Britain	+ 5.1	+14.5	Sep	5.11	4.53	5.08	4.69	4.42	5.73
Canada	+13.6	+ 6.9	Aug	4.17	3.03	4.09	4.18	4.15	5.32
Denmark	+ 8.4	+ 8.0	Sep	3.62	2.25	3.81	3.85	3.30	5.18
Japan	+ 1.5	+ 0.6	Sep	0.34	0.02	0.77	1.78	1.55	2.00
Sweden	+ 0.1	+13.7	Aug	2.74	1.46	3.42	3.78	3.22	3.94
Switzerland	- 2.4	+ 1.6	Sep	1.87	0.83	2.08	2.55	1.92	2.65
United States	- 1.1	+ 4.4	Sep	5.23	4.17	4.88	4.77	4.59	5.76
Euro area†	+ 7.2	+ 8.2	Aug	3.54	2.21	3.74	3.84	3.34	4.50

*Narrow: M1 except Britain notes and coin and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.92%, Japan No. 282 1.79%. Central bank rates: US fed funds 5.25%, ECB refinancing 3.25%, BOJ overnight call 0.25%, BOE repo 4.75%. Sources: Bank of Canada, Commerzbank, Danske Bank, Global Insight, JPMorgan Chase, Lehman Brothers, Stockholmsbörsen, UBS, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Oct 26th 2006
From The Economist print edition

2000=100

	Oct 17th	Oct 24th*	% change on one month	% change on one year
Dollar index				
All items	184.7	183.8	+ 6.7	+ 36.0
Food	147.4	148.7	+ 9.5	+ 19.5
Industrials				
All	232.9	229.2	+ 4.5	+ 53.8
Nfa†	139.2	138.7	+ 2.6	+ 2.6
Metals	284.0	278.5	+ 5.1	+ 77.9
Sterling index				
All items	149.8	148.9	+ 8.0	+ 29.7
Euro index				
All items	136.2	135.5	+ 7.8	+ 31.2
Yen index				
All items	203.4	203.7	+ 8.9	+ 41.7
Gold				
$ per oz	587.58	581.18	– 1.8	+ 23.1
West Texas Intermediate				
$ per barrel	58.87	59.34	– 2.9	– 4.8

*Provisional. †Non-food agriculturals.

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Stockmarkets

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From The Economist print edition

Market indices

	Oct 25th	2006 high	2006 low	% change on one week	% change on record high	% change on Dec 30th 2005 in local currency	% change on Dec 30th 2005 in $ terms
Australia (All Ordinaries)	5,324.7	5,324.7	4,708.8	+ 0.8	nil	+13.1	+17.2
Austria (ATX)	4,117.0	4,344.4	3,324.1	+ 1.8	- 5.2	+12.3	+19.8
Belgium (Bel 20)	4,174.2	4,185.2	3,445.1	+ 0.2	- 0.3	+17.6	+25.5
Britain (FTSE 100)	6,214.6	6,214.6	5,506.8	+ 1.0	- 10.3	+10.6	+20.9
Canada (Toronto Composite)	12,341.7	12,487.3	10,904.3	+ 3.1	- 1.2	+ 9.5	+13.7
Denmark (OMXCB)	400.5	400.5	325.0	+ 2.1	nil	+ 8.9	+16.2
France (SBF 250)	3,821.5	3,821.5	3,244.2	+ 1.3	- 13.0	+15.8	+23.5
France (CAC 40)	5,422.3	5,422.3	4,615.4	+ 1.1	- 21.7	+15.0	+22.7
Germany (DAX)*	6,264.9	6,264.9	5,292.1	+ 1.3	- 22.3	+15.8	+23.6
Italy (S&P/MIB)	39,407.0	39,650.0	34,850.0	- 0.2	- 21.4	+10.4	+17.8
Japan (Nikkei 225)	16,699.3	17,563.4	14,218.6	+ 0.3	- 57.1	+ 3.6	+ 2.7
Japan (Topix)	1,653.4	1,783.7	1,458.3	+ 0.9	- 42.7	+ 0.2	- 0.7
Netherlands (AEX)	492.7	493.4	412.9	+ 0.5	- 29.8	+12.8	+20.4
Spain (Madrid SE)	1,487.3	1,487.3	1,156.8	+ 1.7	nil	+28.6	+37.3
Sweden (Affarsvarlden Gen)	344.6	344.6	275.2	+ 1.2	- 13.9	+17.4	+27.6
Switzerland (Swiss Market)	8,682.5	8,697.6	7,154.9	+ 0.7	- 0.2	+14.5	+19.2
United States (DJIA)	12,134.7	12,134.7	10,667.4	+ 1.2	nil	+13.2	+13.2
United States (S&P 500)	1,382.2	1,382.2	1,223.7	+ 1.2	- 9.5	+10.7	+10.7
United States (NASDAQ Comp)	2,356.6	2,370.9	2,020.4	+ 0.8	- 53.3	+ 6.9	+ 6.9
Europe (FTSEurofirst 300)†	1,454.7	1,454.7	1,238.7	+ 0.9	- 14.7	+14.0	+21.7
Euro area (FTSE Euro 100)†	1,240.7	1,240.7	1,050.0	+ 0.8	- 20.0	+13.9	+21.6
World (MSCI)‡	1,421.2	1,421.2	1,243.9	+ 1.4	- 1.9	+13.0	+13.0
World bond market (Citigroup)††	639.7	653.7	612.1	+ 0.2	- 4.0	+ 3.1	+ 3.1

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Oct 26th 2006
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		Current-account balance The Economist poll % of GDP, forecast 2006	Current-account balance The Economist poll % of GDP, forecast 2007	Exchange rate trade-weighted† 2000=100 Oct 25th	Exchange rate trade-weighted† 2000=100 year ago	Currency units per $ Oct 25th	Currency units per $ year ago	Currency units per £	Currency units per euro	Currency units per ¥100	Budget balance % of GDP 2006‡
Australia	− 10.6	Aug	− 41.0	Q2	− 5.6	− 5.3	119.1	118.4	1.32	1.33	2.47	1.66	1.10	+ 0.9
Austria	− 1.6	Jul	+ 9.2	Q2	+ 0.8	+ 0.8	105.8§	105.1	0.79	0.83	1.49	–	0.67	− 1.9
Belgium	+ 15.9	Aug	+ 6.5	Jun	+ 1.8	+ 2.0	107.6§	106.8	0.79	0.83	1.49	–	0.67	− 0.4
Britain	−142.0	Aug	− 64.4	Q2	− 2.7	− 3.0	102.3	99.3	0.53	0.56	–	0.67	0.45	− 3.4
Canada	+ 57.8	Aug	+ 28.6	Q2	+ 1.5	+ 1.0	128.4	124.1	1.13	1.17	2.11	1.42	0.94	+ 2.2
Denmark	+ 7.9	Aug	+ 7.0	Aug	+ 1.9	+ 1.8	106.5	106.0	5.92	6.18	11.1	7.45	4.97	+ 3.3
France	− 35.0	Aug	− 39.8	Aug	− 1.8	− 1.4	108.5§	107.5	0.79	0.83	1.49	–	0.67	− 2.9
Germany	+185.9	Aug	+105.5	Aug	+ 3.6	+ 3.6	110.2§	108.9	0.79	0.83	1.49	–	0.67	− 3.1
Italy	− 25.5	Aug	− 34.6	Aug	− 1.8	− 1.7	108.1§	107.1	0.79	0.83	1.49	–	0.67	− 4.2
Japan	+ 78.9	Aug	+166.9	Aug	+ 3.5	+ 3.5	79.0	82.8	119	116	224	150	–	− 5.2
Netherlands	+ 38.2	Aug	+ 46.2	Q2	+ 6.3	+ 6.0	108.5§	107.5	0.79	0.83	1.49	–	0.67	− 0.5
Spain	−104.9	Jul	− 97.1	Jul	− 8.4	− 8.0	105.9§	105.3	0.79	0.83	1.49	–	0.67	+ 1.1
Sweden	+ 19.1	Sep	+ 24.1	Q2	+ 6.5	+ 6.0	98.4	94.3	7.32	7.87	13.7	9.22	6.15	+ 1.7
Switzerland	+ 8.8	Sep	+ 55.3	Q2	+13.0	+12.5	104.5	106.8	1.27	1.28	2.38	1.59	1.06	− 0.2
United States	−850.9	Aug	−838.1	Q2	− 6.6	− 6.6	84.6	86.3	–	–	1.88	1.26	0.84	− 3.6
Euro area	− 24.6	Aug	− 44.1	Aug	− 0.4	− 0.2	118.3	116.0	0.79	0.83	1.49	–	0.67	− 2.3
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 11.1	Aug	+ 11.8	Aug	na	na	109.2§	108.3	0.79	0.83	1.49	–	0.67	+ 2.2
Greece	− 39.5	Jul	− 26.1	Aug	na	na	105.0§	104.3	0.79	0.83	1.49	–	0.67	− 3.0
Iceland	− 1.9	Aug	− 3.4	Q2	na	na	85.6**	100.9	68.2	60.4	128	85.9	57.3	+ 2.0
Ireland	+ 37.4	Aug	− 6.0	Q2	na	na	113.9§	112.4	0.79	0.83	1.49	–	0.67	− 0.3
Luxembourg	− 5.3	Jul	+ 4.2	Q2	na	na	107.6§	106.8	0.79	0.83	1.49	–	0.67	− 1.7
New Zealand	− 4.4	Aug	− 10.2	Q2	na	na	130.7	140.0	1.51	1.42	2.84	1.90	1.27	+ 4.6
Norway	+ 59.8	Sep	+ 56.5	Q2	na	na	105.4	112.2	6.61	6.47	12.4	8.32	5.55	+ 18.5
Portugal	− 22.5	Jul	− 16.4	Aug	na	na	105.9**	105.0	0.79	0.83	1.49	–	0.67	− 5.0

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, August average. ‡OECD forecast. **IMF, June average.

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The Economist food index

Oct 26th 2006
From The Economist print edition

Led by higher grain and soya prices, our food index has reached a nine-year high. Drought will cut Australia's wheat harvest by more than half in 2006-07. End-season world grains stocks will be the lowest for 29 years.

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Overview

Oct 26th 2006
From The Economist print edition

South Africa's consumer-price inflation rate eased to 5.3% in September. Inflation excluding mortgage-rate changes, the central bank's target measure, rose to 5.1%, the highest for three years.

South Korea's GDP expanded by 0.9% in the third quarter and by 4.6% in the past year.

In the same quarter, **Russia's** 12-month current-account surplus grew to $101.4 billion.

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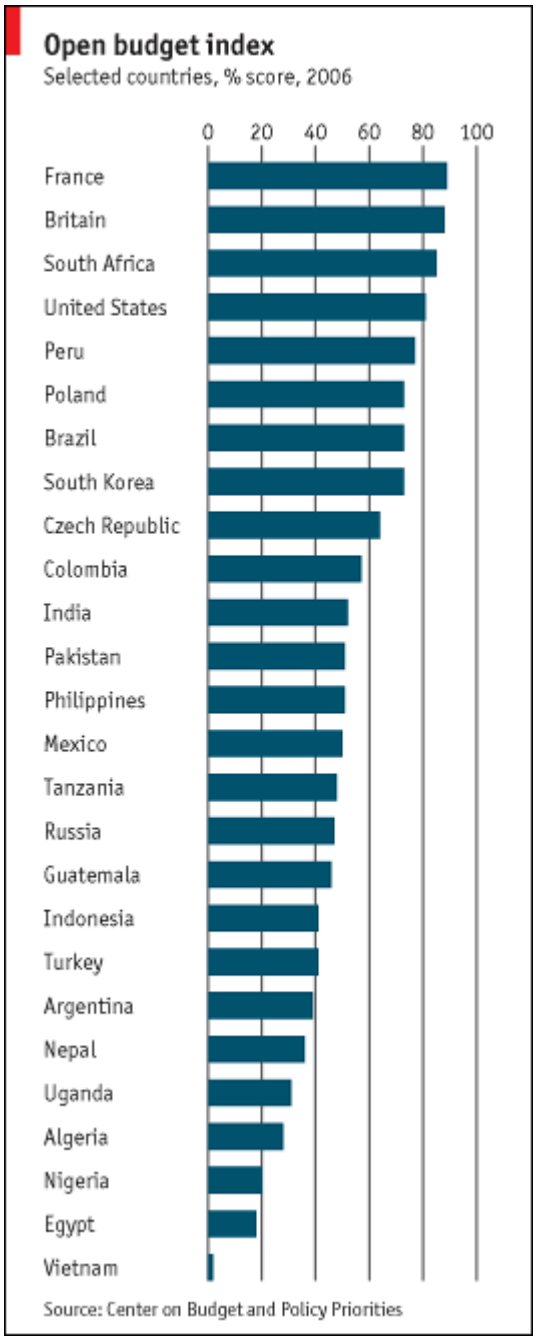
Open budget index

Oct 26th 2006
From The Economist print edition

Citizens should be wary if a government conceals its spending. Some countries reveal more about their budgets than others. France, Britain, America and South Africa are among the countries that provide the most information, according to the new Open Budget Index, created by the Center on Budget and Policy Priorities. The index ranks countries by budget documents published in a year. Nigeria, Egypt and Vietnam provide scant information or none at all.



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Economy

Oct 26th 2006
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+10.4	Q3	+16.1	Sep	+ 1.5	Sep	+143.6	Sep	+160.8	2005	987.9	Sep
Hong Kong	+ 5.2	Q2	+ 5.3	Q2	+ 2.1	Sep	−14.9	Aug	+18.6	Q2	130.3	Sep
India	+ 8.9	Q2	+ 9.7	Aug	+ 6.3	Aug	−41.8	Aug	−13.2	Q2	158.3	Sep
Indonesia	+ 5.2	Q2	+12.2	Jul	+14.5	Sep	+36.4	Aug	+ 4.1	Q2	40.8	Sep
Malaysia	+ 5.9	Q2	+ 5.0	Aug	+ 3.3	Sep	+28.0	Aug	+20.0	Q2	79.0	Aug
Pakistan	+ 6.6	2006†	+13.0	Jul§	+ 8.7	Sep	−12.6	Aug	− 5.0	Q2	11.3	Aug
Philippines	+ 5.5	Q2	− 7.0	Aug	+ 5.7	Sep	− 4.1	Jul	+ 4.3	Jun	18.8	Sep
Singapore	+ 7.1	Q3	+ 7.6	Sep	+ 0.4	Sep	+33.7	Sep	+38.3	Q2	129.4	Sep
South Korea	+ 4.6	Q3	+10.6	Aug	+ 2.4	Sep	+15.6	Sep	+ 5.8	Aug	228.2	Sep
Taiwan	+ 4.6	Q2	+ 2.1	Sep	− 1.2	Sep	+21.7	Sep	+20.6	Q2	261.6	Sep
Thailand	+ 4.9	Q2	+ 7.4	Aug	+ 2.7	Sep	− 1.9	Aug	+ 3.4	Aug	57.7	Aug
Argentina	+ 7.9	Q2	+ 5.7	Aug	+10.4	Sep	+11.5	Sep	+ 7.4	Q2	26.3	Aug
Brazil	+ 1.2	Q2	+ 3.2	Aug	+ 3.7	Sep	+46.3	Sep	+13.3	Sep	70.8	Sep
Chile	+ 4.5	Q2	+ 1.2	Aug	+ 2.8	Sep	+20.0	Sep	+ 2.2	Q2	17.6	Sep
Colombia	+ 6.0	Q2	+12.5	Aug	+ 4.6	Sep	+ 0.7	Jul	− 2.2	Q2	14.9	Sep
Mexico	+ 4.7	Q2	+ 5.8	Aug	+ 4.1	Sep	− 5.3	Sep	− 0.6	Q2	83.6	Aug
Peru	+ 9.2	Aug	+ 9.9	Aug	+ 2.0	Sep	+ 7.4	Aug	+ 1.3	Q2	14.3	Aug
Venezuela	+ 9.2	Q2	+ 7.8	Jul	+15.3	Sep	+37.2	Q2	+29.5	Q2	27.6	Aug
Egypt	+ 5.9	Q1	+ 4.0	2005†	+ 9.6	Sep	−11.2	Q1	+ 2.1	Q1	22.9	Sep
Israel	+ 6.2	Q2	+ 8.1	Aug	+ 1.3	Sep	− 7.5	Sep	+ 5.8	Q2	27.8	Sep
Saudi Arabia	+ 6.6	2005‡	na		+ 2.2	Jul	+126.5	2005	+90.7	2005	25.4	Aug
South Africa	+ 3.6	Q2	+ 4.2	Aug	+ 5.3	Sep	− 8.2	Aug	−13.3	Q2	22.3	Sep
Czech Republic	+ 6.2	Q2	+ 7.4	Aug	+ 2.7	Sep	+ 1.7	Aug	− 3.8	Q2	30.4	Sep
Hungary	+ 3.8	Q2	+ 9.0	Aug	+ 5.9	Sep	− 3.1	Aug	− 7.6	Q2	20.9	Sep
Poland	+ 5.5	Q2	+11.7	Sep	+ 1.6	Sep	− 3.6	Aug	− 6.6	Aug	46.7	Sep
Russia	+ 7.4	Q2	+ 4.1	Sep	+ 9.6	Sep	+142.3	Aug	+101.4	Q3	258.7	Sep
Turkey	+ 7.5	Q2	+ 4.8	Aug	+10.6	Sep	−50.6	Aug	−30.1	Aug	58.0	Aug
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+12.0	Q2	+10.6	Aug	+ 3.8	Sep	− 2.9	Jul	− 1.9	Aug	2.3	Aug
Latvia	+10.9	Q2	+ 7.6	Aug	+ 5.9	Sep	− 4.1	Aug	− 3.1	Aug	3.9	Aug
Lithuania	+ 7.7	Q2	na		+ 3.2	Sep	− 4.4	Aug	− 2.6	Aug	4.1	Aug
Slovakia	+ 6.2	Q2	+13.7	Aug	+ 4.6	Sep	− 3.1	Aug	− 4.4	Jun	12.5	Aug
Slovenia	+ 4.9	Q2	+10.9	Aug	+ 2.5	Sep	− 1.8	Aug	− 0.7	Aug	7.7	Jul

*Excluding gold, except Singapore and China; IMF definition. †Year ending June. ‡Economist Intelligence Unit estimate. §New series.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Oct 26th 2006
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Oct 25th		Dec 30th 2005	
	Oct 25th	year ago	Oct 25th	% a year		one week	in local currency	in $ terms
China	7.90	8.09	14.8	3.00	1,897.9	+1.1	+ 55.4	+ 58.8
Hong Kong	7.78	7.75	14.6	4.14	18,157.9	+0.6	+ 22.1	+ 21.6
India	45.4	45.0	85.1	6.63	12,623.3	- 1.8	+ 34.3	+ 33.3
Indonesia	9,165	9,992	17,202	10.92	1,572.8	+0.5	+ 35.3	+ 45.2
Malaysia	3.68	3.77	6.90	3.80	979.2	+0.3	+ 8.8	+ 11.9
Pakistan	60.6	59.7	114	10.30	11,565.3	+1.5	+ 21.0	+ 19.5
Philippines	50.0	55.0	93.8	7.81	2,678.7	+5.2	+ 27.8	+ 35.7
Singapore	1.57	1.69	2.95	3.44	2,714.7	+2.7	+ 15.6	+ 22.4
South Korea	956	1,046	1,794	4.61	1,371.4	+1.3	- 0.6	+ 5.1
Taiwan	33.3	33.7	62.5	1.84	7,059.9	+0.6	+ 7.8	+ 6.4
Thailand	37.1	40.8	69.6	5.25	732.8	+2.0	+ 2.7	+ 13.5
Argentina	3.09	2.99	5.80	10.13	1,644.7	- 2.8	+ 6.6	+ 4.3
Brazil	2.15	2.27	4.04	13.67	36,105.0	- 6.7	+ 7.9	+ 17.0
Chile	524	547	984	5.16	10,641.6	- 3.0	+ 15.6	+ 12.9
Colombia	2,341	2,288	4,393	6.43	9,121.9	- 6.4	- 4.1	- 6.3
Mexico	10.8	10.9	20.3	7.04	21,748.6	- 5.5	+ 22.2	+ 20.4
Peru	3.23	3.39	6.06	4.50	10,343.8	- 4.3	+115.4	+129.0
Venezuela	2,881§	2,834§	5,408	10.00	34,926.7	- 6.3	+ 71.3	+ 53.7
Egypt	5.74	5.76	10.76	9.56	57,361.2	+0.9	+ 3.6	+ 3.7
Israel	4.29	4.63	8.05	5.36	895.0	+0.7	+ 8.1	+ 16.0
Saudi Arabia	3.75	3.75	7.04	5.22	10,545.4	nil	- 36.9	- 36.9
South Africa	7.61	6.69	14.3	8.65	23,489.5	+1.2	+ 29.8	+ 8.2
Czech Republic	22.5	24.7	42.3	2.67	1,562.4	+3.2	+ 6.1	+ 15.9
Hungary	209	209	392	8.17	22,634.4	+0.5	+ 8.9	+ 11.7
Poland	3.09	3.29	5.81	4.20	47,951.5	+0.6	+ 34.7	+ 41.8
Russia	26.9	28.5	50.5	11.00	1,630.5‡	+0.2	+ 35.5	+ 44.9
Turkey	1.47	1.36	2.75	20.22	39,643.8	- 0.3	- 0.3	- 8.2
EM (MSCI)*	1.00	1.00	1.88	na	776.0	- 3.7	+ 9.8	+ 9.8
EMBI+†	1.00	1.00	1.88	na	391.2	- 1.1	+ 6.1	+ 6.1

*Emerging Mkts. †JPMorgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Trading market value.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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